

Board Meeting Agenda

26 July 2017
9.15 am to 5.00pm

Manners Street, Wellington

Est. Time	Item	Topic	Objective		Page
A: NON-PUBLIC SESSION					
B: PUBLIC SESSION					
10:30 am	3	<u>ISA 540 submission (Late Papers)</u>			
	3.1	Board meeting summary paper	Note	Paper	Late paper
	3.2	Draft submission	Approve	Paper	Late paper
	3.3	OAG Submission	Note	Paper	Late paper
	3.4	IAASB ED	Consider	Paper	Late paper
11:30 am	4	<u>Auditor reporting FAQs</u>			
	4.1	Board meeting summary paper	Note	Paper	
	4.2	Additional FAQs	Approval	Paper	
	4.3	ASA 2017 -1 Amendments to Australian Auditing Standards	Note	Paper	
12:00 pm	5	<u>Auditor Reporting – Joint report</u>			
	5.1	Board meeting summary paper	Note	Paper	
	5.2	Overview of joint project	Note	Paper	
	5.3	Draft questionnaires	Consider	Paper	
	5.4	Initial feedback from NZ Shareholders Association	Note	Paper	
12:30 pm	6	<u>Meet with FMA (Rob Everett)</u>			
1:00 pm	<i>Lunch</i>				
1.45 pm	7	<u>IESBA ED Professional scepticism</u>			
	7.1	Board meeting summary paper	Note	Paper	
	7.2	Draft submission	Approve	Paper	
	7.3	KPMG submission to the NZAuASB	Note	Paper	
	7.4	IESBA exposure draft	Consider	Paper	
2:05 pm	8	<u>Long association FAQs</u>			
	8.1	Board meeting summary paper	Note	Paper	
	8.2	Draft FAQs	Approve	Paper	
	8.3	IESBA FAQs	Note	Paper	
2:35 pm	9	<u>Guidance for prescribers of assurance requirements</u>			
	9.1	Board meeting summary paper	Note	Paper	
	9.2	Draft guidance	Consider	Paper	
3.00 pm	<i>Afternoon tea</i>				
C: NON-PUBLIC SESSION					

Next meeting: 6 September 2017, Wellington

NZAuASB Board Meeting Summary Paper

AGENDA ITEM NO.	4.1
Meeting date:	26 July 2017
Subject:	Frequently asked questions – auditor reporting
Date:	3 July 2017
Prepared by:	Misha Pieters

Action Required

For Information Purposes Only

Agenda Item Objectives

To CONSIDER adding additional frequently asked questions (FAQs) regarding auditor reporting implementation matters to the website.

Background

1. The NZAuASB approved a series of FAQs related to the revised auditor reporting requirements at the February Board meeting. These are available on the new XRB website at <https://www.xrb.govt.nz/standards-for-assurance-practitioners/new-auditors-report/frequently-asked-questions>.
2. Further implementation questions have arisen as more auditors apply the revised requirements to all audit engagements. The AUASB has considered further issues with respect to reporting of key audit matters, for example in group and parent financial statements and stapled security issuers. In January 2017, the AUASB proposed to make amendments to the ASAs. In May, the AUASB approved limited amendments to the ASAs but has not included all of the proposals that were exposed. The amendments the AUASB approved are at agenda item 4.3 for the information of the Board.
3. The NZAuASB has considered the AUASB proposals at its February meeting and agreed that there were no compelling reasons to amend the ISAs (NZ). The key changes being added in Australia are to:
 - a. Reinstate the Aus paragraph from the previous version of ASA 700 *Forming an Opinion and Reporting on a Financial Report* in relation to the date the auditor's report is signed;
As discussed by the NZAuASB in February there is not a compelling reason to amend the ISAs in New Zealand.

- b. Achieve consistency in relation to naming of the engagement partner, between application material contained within ASA 800 *Special Considerations—Audits of Financial Statements Prepared in Accordance with Special Purpose Frameworks* and ASA 805 *Special Considerations—Audits of Single Financial Statements and Specific Elements, Accounts or Items of a Financial Statement* and a requirement within ASA 700;

ASA 700 para Aus 46.1 has been amended and requires “The name of the engagement partner shall be included in the auditor’s report where required by law or regulation”.

The ISA and ISA (NZ) 700 (Revised) requires the name of the engagement partner shall be included in the auditor’s report on financial statements of listed entities or FMC reporting entities considered to have a higher level of public accountability unless, in rare circumstances, such disclosure is reasonably expected to lead to a significant personal security threat.

Since no change has been made to ISA (NZ) 700 (Revised), no compelling reason changes are identified for ISA (NZ) 800 and ISA (NZ) 805.

- c. Provide internal consistency in relation to numbering and internal referencing within ASA 800 and ASA 805.
4. In addition, further FAQs have been approved by the AUASB to address implementation matters identified. There are even further matters identified that are under discussion and may result in further FAQs being added at a later stage.
 5. We have considered the additional FAQs approved by the AUASB and consider that these are relevant and helpful in the New Zealand context. We recommend adding additional FAQs to the XRB website. The amendments and additions are outlined in agenda item 4.2.

Action

6. We request APPROVAL from the Board to add the additional FAQs to the XRB website.

Material Presented

Agenda item 4.1	Board Meeting Summary Paper
Agenda item 4.2	Amendments to and additional FAQs for approval
Agenda item 4.3	Amendments to Australian Auditing Standards

Issues paper: Amendments to and additional frequently asked questions

1. This issues paper considers amendments to existing frequently asked questions (FAQs) and potential additional questions to add to the Auditor Reporting Frequently Asked Questions as a result of queries received and matters identified by the AUASB.

Amendments to existing FAQs

2. We have identified 3 existing FAQs where amendments may be useful:
 1. How many KAMs to report?
 2. Parent and group financial statements
 3. When to identify the other information

Does the Board agree with the additions and edits outlined in the following paragraphs?

3. The AUASB considered the additional questions added in New Zealand, which have not been covered in Australia. Some feedback was received regarding the question on the number of Key audit matters (KAMs) to report, including whether the use of the term “must” was too prescriptive, and the appropriateness of the sentence that implies that more complex entities are more likely to have more KAMs. As practice is emerging, this is not always proving to be the case. We have marked up some recommended edits to the existing question and response:

4. How many KAMs ~~should~~ must be reported?

There is no specific guidance on how many KAMs should be communicated. ‘Early adopter’ reports issued to date in New Zealand, contained between 1 and 5 KAMs with an average of around 3 KAMs. ~~For audits of more complex entities it may be appropriate to have more KAMs than for a non-complex entity.~~ Other matters that may impact the number of KAMs communicated are the nature of an entity’s business and environment. The intention however, is to communicate the areas of most significance in the audit and a long list of matters may detract from this.

4. The AUASB had proposed to amend ASA 701 to provide guidance that KAMs were not required for parent financial statements. Based on feedback received, these proposals have not been adopted, i.e. there will be no change to the ASAs. The AUASB had not covered this matter in their previous FAQs but have now approved a question on this matter.

5. The NZAuASB had added a question, based on the FAQs published by the International Auditing and Assurance Standards Board (IAASB). The AUASB has adopted a slightly different style to responding to this question. We consider that the New Zealand FAQ does not need to be amended to align exactly with the AUASB response, but has identified some further additions to the existing New Zealand response, based on material developed by the AUASB. These are marked up below:

Q:27. Where the auditor is required to express an audit opinion on the separate financial statements of a parent or holding company, and the auditor is required to communicate KAM, is the auditor also required to communicate KAM in respect of the separate financial statements?—How are KAMs communicated for consolidated and parent financial statements?

A: ISA (NZ) 701 indicates that the standard applies to audits of complete sets of general purpose financial statements of FMC reporting entities considered to have a higher level of public accountability. ISA (NZ) 700 (Revised) states “the requirements of the applicable financial reporting framework determine the form and content of the financial statements, and what constitutes a complete set of financial statements”.

....

In circumstances where the separate financial statements are not a complete set of general purpose financial statements under the applicable financial reporting framework, the auditor could voluntarily communicate KAM. [For example, parent entity financial information is usually presented within consolidated group financial statements by way of a note.](#)

[In consolidated financial statements, which includes parent entity information in a note only, KAMs do not need to be identified and communicated separately for the parent entity. However, if there is a matter relative to the parent entity which is considered to be a KAM at the consolidated financial statements level, the auditor communicates this in the auditor’s report on the consolidated financial statements.](#)

...

There are a variety of possible scenarios regarding the presentation of the consolidated and separate financial statements and the related auditor’s report, with resulting implications for how KAM are communicated and presented in these circumstances. For example, the consolidated and separate financial statements could be presented in completely separate annual reports, presented as discrete financial statements in a single document (e.g., in separate sections of a single annual report), or presented combined in a single annual report (also known as a four-column format). [For example, if an entity elects to prepare 4 column consolidated financial statements including general purpose parent entity financial statements, they must be prepared in accordance with the New Zealand Accounting](#)

[Standards. The auditor identifies and communicates KAMs addressing the audits for both the parent entity and the consolidated entity separately.](#)

...

If the financial statements are presented in a single document (columnar format) because the auditor in this case would likely issue a single auditor's report addressing both the consolidated and separate financial statements, the single report would include KAM relating to the audits of both sets of financial statements. This could be presented in a variety of ways, for example:

- Indicating for each KAM how it applies to each audit, i.e., the audit of the consolidated and separate financial statements
- Presenting the KAM for the consolidated financial statements in one section, and those for the separate financial statements in another section (the auditor could cross-refer to the related KAM in the respective sections if the auditor believes it appropriate to do so).

[If in the auditor's judgement there are no KAMs relevant to the parent entity \(e.g., if the parent entity has limited operations\) the auditor's report reflects this as:](#)

Key Audit Matters

[We have determined there are no Key Audit Matters to communicate in our report for the parent entity.](#)

[If the parent entity prepares a separate set of special purpose financial statements, KAMs are not required to be communicated.](#)

6. New Zealand practitioners have highlighted the need for additional guidance in applying the revisions to ISA (NZ) 720. The AUASB has added an additional question – which we consider is covered by the New Zealand response in the table outlined below. However, there is additional clarification on when or why the auditor would identify the information. We recommend adding the wording below, as this provides useful addition guidance.

When is the auditor's report required to include an Other Information section?

Information received	FMC reporting entities considered to have a higher level of public accountability	Other entities (Not a FMC reporting entity considered to have a higher level of public accountability)
The auditor has received some or all of the other	√	√

Information received	FMC reporting entities considered to have a higher level of public accountability	Other entities (Not a FMC reporting entity considered to have a higher level of public accountability)
information at the date of the auditor's report	Identify information obtained prior to the date of the auditor's report	
The auditor has not received any other information at the date of the auditor's report but expects to receive this information at a later date	<p style="text-align: center;">√</p> Identify information not yet obtained but expected to be obtained after the date of the auditor's report	Voluntary reporting If no information has been received, the auditor's report is not required to include an Other Information section

It is not uncommon for an entity to prepare its full annual report after the audit opinion on the financial statements have been signed by the auditor. In this scenario the auditor's report for a FMC reporting entity considered to have a higher level of public accountability details the other information which is expected to be received after the date of the auditor's report.

[When detailing the other information received, and not yet received for FMC reporting entities considered to have a higher level of public accountability, the auditor can refer to the specific name of the documents to avoid any confusion as to the other information which the auditor has read and considered as at the date of the auditor's report.](#)

Additional FAQs for consideration in the New Zealand context

- The Board is asked for feedback as to whether the following additional questions, identified by the AUASB, should be added under the appropriate sections in the existing FAQs as follows:

Changes to the Auditor's Report

Key Audit Matters

Auditor's Responsibility Statements

1. How does the auditor's responsibility statements differ for different types of entities?

The auditor's responsibilities section in the auditor's report differs depending on the type of entity being audited:

All auditor's reports include the content required by ISA (NZ) 700 (Revised) paragraphs 37, 38 and 39 (a) and (b)(i) to (iv), and 40(a).

ISA (NZ) 700 (Revised) paragraph 39 (b) (v) is applicable for auditor's reports of financial statements prepared in accordance with a fair presentation framework.

ISA (NZ) 700 (Revised) paragraph 39 (c) is applicable for audits where ISA (NZ) 600 applies.

ISA (NZ) 700 (Revised) paragraph 40 (b) is applicable for audits of FMC reporting entities considered to have a higher level of public accountability and relates to communication with those charged with governance related to compliance with relevant ethical requirements.

ISA (NZ) 700 (Revised) paragraph 40(c) is applicable for audits for which key audit matters are communicated.

Where service performance information is included within the scope of the audit, additional matters will be covered in the auditor's responsibility statements.

2. How does the auditor make reference to the auditor's responsibilities statement on the XRB website?

Auditor's may elect to present parts of the auditor's responsibility section (ISA (NZ) 700 (Revised), paragraph 41) by including a reference within the Auditor's Report to a specific webpage on the External Reporting Board's (XRB) website.

In this scenario the auditor's report refers to the specific webpage that applies to the auditor's responsibilities applicable in the context of the engagement. (ISA (NZ) 700 (Revised), paragraph NZ A57.1).

When referring to the responsibilities statements the auditor includes the URL <https://www.xrb.govt.nz/standards-for-assurance-practitioners/auditors-responsibilities/audit-report-#/> (where # represents the specific number of the relevant statement).

The URL has recently changed as a result of the XRB website upgrade. References to the URL from the old website still work and automatically redirect to the new XRB website.

No responsibility section has been added to the XRB website for an auditor to refer to where the audit includes the audit of service performance information. Such responsibilities will be added once the NZAuASB has completed its project to develop an auditing standard on the audit of service performance information.

Other Information

3. How does the auditor determine the documents that comprise the annual report?

The annual report contains or accompanies the financial statements and the auditor's report thereon. This may be a single document or a combination of documents that are prepared to provide owners with information on the entity's operations, financial results and financial position.

The annual report includes material required by statutory and regulatory requirements (for example, NSX listing rules) and may include additional voluntary reporting.

Determining the documents that comprise the annual report is often clear as they are required by statutory and regulatory requirements, or are within the one document called "Annual Report".

If this is not the case the auditor uses professional judgement when determining what comprises the annual report considering the timing, purpose of the documents and for whom they are intended.

Going Concern

4. What is included in the "Material Uncertainty Related to Going Concern" paragraph in the auditor's report?

If there is a material uncertainty related to going concern, and adequate disclosure in the financial statements, the auditor's report includes a section which is now required to be titled "Material Uncertainty Related to Going Concern" (MURGC) (i.e., no longer as an Emphasis of Matter).

ISA (NZ) 570 (Revised) Going Concern, paragraph 22 establishes the minimum information to be presented in the auditor's report under the MURGC heading which is to:

- Draw attention to the note in the financial statements which includes the required disclosures; and
- State that these events or conditions indicate that a material uncertainty exists that may cast significant doubt on the entity's ability to continue as a going concern, and that the auditor's opinion is not modified in respect of the matter.

Sample wording is contained in Illustration 1 of the Appendix 2 of ISA (NZ) 570 (Revised).

A MURGC is by its nature a KAM, however the MURGC is to be reported in a separate section of the auditor's report. The introductory sentences to the KAM section of the

auditor's report includes a cross reference to the MURGC section, where the matter is described.

The description of the matter required to be included in the MURGC section is less than what is required in the KAM section of the auditor's report. However, the auditor may provide additional information in the MURGC section to supplement the required ISA (NZ) 570 (Revised) paragraph 22 statements, for example to explain;

- That the existence of a material uncertainty is fundamental to user's understanding of the financial statements, or
- How the matter was addressed in the audit .

If there is an event or condition which may cast significant doubt on the entity's ability to continue as a going concern, but the auditor concludes the uncertainty is not material and that the use of the going concern assumption is appropriate, no additional disclosure or additional paragraph in the auditor's report is required. However, the auditor considers whether this is a KAM in accordance with ISA (NZ) 701 *Communicating Key Audit Matters*, paragraphs 9 and 10.

Special Purpose Financial Statements

5. Are auditor's reports on special purpose financial statements impacted by the changes to the auditor's report?

ISA (NZ) 800 (Revised) *Special Considerations – Audits of Financial Statements Prepared in Accordance with Special Purpose Frameworks* has been revised to reflect the changes to auditor reporting.

Auditor's reports on special purpose financial statements are not within the scope of ISA (NZ) 701, and therefore there is no requirement for the auditor to communicate KAMs unless required by law or regulation. However, the auditor may elect to communicate KAMs.

ISA (NZ) 720 (Revised) deals with the auditor's responsibilities relating to other information. Reports containing or accompanying special purpose financial statements with the purpose of providing owners with information on matters presented in the special purpose financial statements, are considered to be annual reports, and the requirements in ISA (NZ) 720 (Revised) apply. (ISA (NZ) 800 (Revised), paragraph A17).

Summary Financial Statements

6. Do auditor's reports on summary financial statements include communication of key audit matters?

ISA (NZ) 810 (Revised) *Engagements to Report on Summary Financial Statements* has been revised to reflect the changes to auditor reporting.

Where the auditor's report on the complete financial statements includes KAMs, the auditor's report on the summary financial statements states that the auditor's report on the complete financial statements includes communication of KAMs.

The intention is to draw to the users' attention that there are KAMs in the auditor's report on the complete financial statements, however the auditor is not required to describe in detail or repeat the KAMs in the auditor's report on the summary financial statements.

7. What is the auditor's responsibility in relation to information in documents containing summary financial statements?

For audits of summary financial statements, the auditor complies with the requirements of ISA (NZ) 810 (Revised) *Engagements to Report on Summary Financial Statements*.

ISA (NZ) 810 (Revised) requires the auditor to read and consider the information included in documents containing summary financial statements, and consider whether there is a material inconsistency between that information and the summary financial statements. (ISA (NZ) 810 (Revised), paragraph 14).

If the auditor identifies a material inconsistency, the auditor discusses this with management and determines whether the summary financial statements or the information included in the document containing the summary financial statements needs to be revised. If management does not make appropriate amendments to address the material inconsistency, the auditor considers the impact on the auditor's report. (ISA (NZ) 810 (Revised), paragraph 15).

If the other information included with summary financial statements, is the same as the other information included in the annual report, the work already performed by the auditor in accordance with ISA (NZ) 720 (Revised) may be adequate.

If the other information included with summary financial statements, is not included in the annual report, the auditor may still find the requirements of ISA (NZ) 720 (Revised) helpful, and follows the requirements of ISA (NZ) 810 (Revised) detailed above.

Possible additional FAQs to be developed

8. The AUASB have identified some potential further matters to address in FAQs. We agree that all of these matters would be useful to discuss and provide further clarification about. We will continue to monitor developments and consider we should work closely with AUASB staff to develop appropriate responses.
9. Examples of possible additional matters to be dealt with include:

- When a client becomes listed after year end date, but before the audit report date, are KAMs communicated?
- Given references have been amended to refer to directors having responsibility, on behalf of the entity, for the preparation of the financial statements, should KAMs avoid the term "management" when discussing origination of estimates, etc?
- What is the interpretation of "current period" for application in paragraph 10 of ISA (NZ) 701? For instance, where a non-adjusting subsequent event is identified, are KAMs communicated/included?
- Are references to the going concern assessment applicable for Tier 4 entities (and therefore whether the Directors & Auditors responsibilities should include the going concern responsibilities)?
The use of 'cash basis' may be ambiguous as to whether it is really getting at cash in cash out (no residual obligation to distribute/accrue leftover cash) presentation of the Statement. If it is cash in cash out, there is an argument that teams would not consider going concern as there is no intent in the Statement that 'continuity of business' (going concern) is relevant.

ISA (NZ) 570 (Revised) states: "In other financial reporting frameworks, there may be no explicit requirement for management to make a specific assessment of the entity's ability to continue as a going concern. Nevertheless, where the going concern basis of accounting is a fundamental principle in the preparation of financial statements as discussed in paragraph 2, the preparation of the financial statements requires management to assess the entity's ability to continue as a going concern even if the financial reporting framework does not include an explicit requirement to do so."

In addition "These responsibilities exist even if the financial reporting framework used in the preparation of the financial statements does not include an explicit requirement for management to make a specific assessment of the entity's ability to continue as a going concern".

- How do the revised amendments impact on review reports?
 - Is it acceptable to use "Material uncertainty regarding going concern" language instead of Emphasis of matter language in a half year review, even though NZ SRE 2410 has not updated?
 - Is it acceptable to reorder review reports consistent with ISA (NZ) 700 (Revised) re-ordering of the audit report?

Staff have previously raised the need to consider the implications of the revisions on NZ SRE 2410.

- Clarification on the footnote in ISA 720 illustrative examples. The footnote states:
"It may be useful to include an additional paragraph in the other information section of the auditor's report when the auditor has identified an uncorrected material misstatement of the other information obtained

after the date of the auditor's report and has a legal obligation to take specific action in response."

The following is what would be included in that instance
"When we read the Y report, if we conclude that there is a material misstatement therein, we are required to communicate that matter to those charged with governance and [describe actions applicable]."

Staff have sought clarification from IAASB staff as to why this footnote was included and how this would be applied in practice, given that at the date of the report, the auditor has not received that information and therefore has no idea whether it is misstated or not.

ASA 2017-1
(April 2017)

Auditing Standard ASA 2017-1 *Amendments to Australian Auditing Standards*

Issued by the **Auditing and Assurance Standards Board**



Australian Government

Auditing and Assurance Standards Board

Obtaining a Copy of this Auditing Standard

This Auditing Standard is available on the Auditing and Assurance Standards Board (AUASB) website: www.auasb.gov.au

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PREFACE

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CONFORMITY WITH INTERNATIONAL STANDARDS ON AUDITING

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PREFACE

Reasons for Issuing ASA 2017-1

The AUASB issues Auditing Standard ASA 2017-1 *Amendments to Australian Auditing Standards* pursuant to the requirements of the legislative provisions and the Strategic Direction explained below.

The AUASB is a Non Corporate Commonwealth Entity of the Australian Government established under section 227A of the *Australian Securities and Investments Commission Act 2001*, as amended (ASIC Act). Under section 336 of the *Corporations Act 2001*, the AUASB may make Auditing Standards for the purposes of the corporations legislation. These Auditing Standards are legislative instruments under the *Legislative Instruments Act 2003*.

Under the Strategic Direction given to the AUASB by the Financial Reporting Council (FRC), the AUASB is required, inter alia, to develop auditing standards that have a clear public interest focus and are of the highest quality.

Main Features

This Auditing Standard makes amendments to the following Auditing Standards:

- ASA 700 *Forming an Opinion and Reporting on a Financial Report* (1 December 2015)
- ASA 800 *Special Considerations – Audits of Financial Reports Prepared in Accordance with Special Purpose Frameworks* (26 July 2016)
- ASA 805 *Special Considerations – Audits of Single Financial Statements and Specific Elements, Accounts or Items of a Financial Statement* (26 July 2016)

The amendments arise from changes made by the AUASB to address Australian legislative scenarios. These changes have passed the compelling reasons test and are considered appropriate and in the public interest. Under the Strategic Direction given to the AUASB by the Financial Reporting Council (FRC), the AUASB is required to have regard to any programme initiated by the IAASB for the revision and enhancement of the International Standards on Auditing (ISAs) and to make appropriate consequential amendments to the Australian Auditing Standards.

AUTHORITY STATEMENT

The Auditing and Assurance Standards Board (AUASB) makes this Auditing Standard ASA 2017-1 *Amendments to Australian Auditing Standards* pursuant to section 227B of the *Australian Securities and Investments Commission Act 2001* and section 336 of the *Corporations Act 2001*.

Dated: <TypeHere>

R Simnett
Chair - AUASB

Conformity with International Standards on Auditing

This Auditing Standard has been made for Australian legislative purposes and accordingly there is no equivalent International Standard on Auditing (ISA) issued by the International Auditing and Assurance Standards Board (IAASB), an independent standard setting board of the International Federation of Accountants (IFAC). It contains amendments to the Australian Auditing Standards (as shown below).

AUDITING STANDARD ASA 2017-1

Amendments to Australian Auditing Standards

Application

1. This Auditing Standard applies to:
 - an audit of a financial report for a financial year, or an audit of a financial report for a half-year, in accordance with the *Corporations Act 2001*; and
 - an audit of a financial report, or a complete set of financial statements, for any other purpose.
2. This Auditing Standard also applies, as appropriate, to an audit of other historical financial information.

Operative Date

3. This Auditing Standard is operative for financial reporting periods commencing on or after 15 December 2016.

Introduction

Scope of this Auditing Standard

4. This Auditing Standard makes amendments to the Australian Auditing Standards:
 - (a) *ASA 700 Forming an Opinion and Reporting on a Financial Report* (issued 1 December 2015)
 - (b) *ASA 800 Special Considerations – Audits of Financial Reports Prepared in Accordance with Special Purpose Frameworks* (issued 26 July 2016)
 - (c) *ASA 805 Special Considerations – Audits of Single Financial Statements and Specific Elements, Accounts or Items of a Financial Statement* (issued 26 July 2016)

Objective

5. The objective of this Auditing Standard is to make amendments to the following Auditing Standards:
 - (a) *ASA 700 Forming an Opinion and Reporting on a Financial* (1 December 2015)
 - (b) *ASA 800 Special Considerations – Audits of Financial Reports Prepared in Accordance with Special Purpose Frameworks* (26 July 2016)
 - (c) *ASA 805 Special Considerations – Audits of Single Financial Statements and Specific Elements, Accounts or Items of a Financial Statement* (26 July 2016)

Definition

6. For the purposes of this Auditing Standard, the meanings of terms are set out in each Auditing Standard and in the *AUASB Glossary*. This Auditing Standard does not introduce new definitions.

Amendments to Auditing Standards

Amendments to ASA 700

7. New paragraph Aus 49.1 inserted after paragraph 49 as follows:
The auditor's report shall be dated as of the date the auditor signs that report.
8. A footnote is added to the "Auditor's Signature" line in illustrations 1A, 2A, 3 and 4 after the heading as follows:
The date of the auditor's report is the date the auditor signs the report.

Amendments to ASA 800

9. Amend numbering of current paragraph Aus 1.1 to Aus 0.1.
10. Amend numbering of current paragraph Aus 1.2 to Aus 0.2.
11. Amend numbering of current paragraph Aus 1.3 to Aus 0.3.
12. Paragraph A18 and associated footnote is deleted.
13. A new paragraph Aus A18.1 and footnote is inserted as follows:
The requirement in ASA 700 for the name of the engagement partner to be included in the auditor's report where required by law or regulation also applies to audits of special purpose financial reports. (footnote See ASA 700 paragraph Aus 46.1, A61-A63)

Amendments to ASA 805

14. Amend numbering of current paragraph Aus 1.1 to Aus 0.1.
15. Amend numbering of current paragraph Aus 1.2 to Aus 0.2.
16. Amend numbering of current paragraph Aus 1.3 to Aus 0.3.
17. Paragraph A22 and associated footnote is deleted.
18. A new paragraph Aus A22.1 and footnote is inserted as follows:
The requirement in ASA 700 for the name of the engagement partner to be included in the auditor's report where required by law or regulation also applies to audits of single financial statements and specific elements, accounts or items of a financial statement. (footnote See ASA 700 paragraph Aus 46.1, A61-A63)

NZAuASB Board Meeting Summary Paper

AGENDA ITEM NO.	5.1
Meeting date:	26 July 2017
Subject:	Joint report with the FMA on auditor reporting
Date:	30 June 2017
Prepared by:	Misha Pieters

<input checked="" type="checkbox"/> Action Required	<input type="checkbox"/> For Information Purposes Only
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Agenda Item Objectives

For the Board to consider and provide feedback on possible stakeholders to approach and on proposed questionnaires for each stakeholder group to target as part of the joint project with the FMA on the implementation of the new auditor's report.

Background

1. The FMA approached the XRB in 2016 with a proposal to perform a review of the New Zealand experience in implementing the new auditor reporting standards, and to publish a joint report on the outcome of the review.
2. The NZAuASB APPROVED a project plan at the April 2017 board meeting and agreed to consider more detailed plans for roundtables and interviews to be held at the July meeting.
3. In drafting the questionnaires, we have considered the two reports published by the Financial Reporting Council:
 - a. [March 2015](#) Extended auditor's reports – A review of experience in the first year
 - b. [January 2016](#) Extended auditor's reports – A further review of experience.
4. In addition, the Director of Assurance Standards has been in discussions with the Canadians and Australians who are also researching the impact of the revised auditor reporting requirements. This group has developed a draft survey. We have made use of this draft survey in preparing the questionnaires.

Matters to Consider

5. An outline of the contents of the proposed report is available at agenda 5.2, including timeframes and project milestones.
6. The Board has agreed to include responses from practitioners, investors and those charged with governance, in addition to views of the regulator and the standard setter. Proposed outreach and draft questionnaires are available at agenda 5.3, indicating questions to raise with target groups. The board is asked to provide feedback on the proposed questions and target groups.

Material Presented

Agenda item 5.1
Agenda item 5.2
Agenda item 5.3
Agenda item 5.4

Board Meeting Summary Paper
Overview of joint project.
Draft questionnaires for each target group
Initial feedback from New Zealand Shareholder Association Survey

Outline of the proposed joint project by the FMA and the NZAuASB on auditor reporting

Objective

1. The objective of the project is to conduct a review of the New Zealand experience in implementing the new auditor reporting standards, with a view to better understand:
 - the value and benefits of the enhanced auditor reporting for all stakeholders;
 - implementation issues and specific challenges identified, and where further guidance may be needed.

Outcome of the project

2. The outcome of the project will be a joint report by the FMA and the NZAuASB, and will include a review of all final audit reports of listed entities, plus those entities that have adopted to report KAM voluntarily, up to periods ending 30 June 2017. We estimate this will cover approximately 150 listed entities' auditor reports.

Contents

3. The contents of the report will cover:
 - A small section on the international experience
 - Various statistics/infographics, based on an analysis of following data being collected:
 - Entity name and auditor
 - Number of KAMs
 - main KAM topics
 - length of audit reports compared to prior year
 - audit fees over last three years
 - industry
 - conclusions or findings included in KAMs
 - materiality disclosed, and benchmark used
 - type of audit opinion (going concern disclosure, unqualified, disclaimer)
 - View from the standard setter
 - View from the regulator
 - Views from practitioners (some quotes)
 - Views from investors (some quotes)
 - Views from TCWG (some quotes)
 - Experiences and growth of early adopters over two years
4. It is yet to be decided who will produce the report, i.e. the NZAuASB or the FMA. A skeleton report is under consideration.

How the project will be conducted

5. FMA staff will collect and summarise the statistics as they have access to all the reports issued.
6. The NZAuASB staff will conduct targeted interviews/roundtables with key stakeholders: auditors, preparers, investors, and audit committee members.

Timetable

Indicative Timing	Activity	Responsibility
Feb 2017 – Oct 2017	<ul style="list-style-type: none"> Collect statistics on audit reports 	FMA
July 2017	<ul style="list-style-type: none"> Identify potential roundtables and interviewees. Develop questionnaire for each key stakeholder group. Draft skeleton report 	NZAuASB /FMA
Aug 2017- Sept 2017	<ul style="list-style-type: none"> Conduct roundtables and interviews 	NZAuASB
Sept 2017-Oct 2017	<ul style="list-style-type: none"> Draft report 	NZAuASB/FMA
Nov 2017	<ul style="list-style-type: none"> Review of draft report 	NZAuASB/FMA
Dec 2017/Jan 2018	<ul style="list-style-type: none"> Issue final report 	NZAuASB/FMA

7. We will present the following to the Board for feedback during the timeline of the project:

Output	NZAuASB meeting
<ul style="list-style-type: none"> More detailed planning on roundtables and interviews to be conducted during Aug to Sept 2017 Draft questionnaire for each stakeholder group Draft skeleton report 	26 July 2017
<ul style="list-style-type: none"> Feedback on roundtables and interviews conducted, and summary of key statistics collected to date 	25 October 2017
<ul style="list-style-type: none"> Draft report for approval 	13 December 2017

Draft Questionnaires related to auditor reporting experience

Target group: Investors

1. The New Zealand Shareholders Association has recently conducted a survey in order to get initial views of its members about the new auditor's report. The results of this survey is at agenda 5.4.
2. This survey was conducted prior to the June year end. There has only been a limited number of new reports in the market at the time of this survey. We recommend conducting a follow up survey in August to determine whether more investors have had an opportunity to see the new format. Responses to the survey indicate that only 32% of participants had seen the new format.
3. We also suggest targeting institutional investors, possibly analysts at banks and other investment companies and possibly supervisors (i.e. trustees). If the Board has any suggestions on specific people to target, please forward these contacts to staff.
4. We consider a similar format may be appropriate, but have amended and expanded the question on the inclusion of key audit matters (KAMs), exploring issues on materiality and audit findings in the questions. The Shareholders Association may be able to assist us to conduct a similar survey asking similar questions, but expanding more about KAMs:
 - i. Have you had the opportunity to see the new auditor's report format yet?
 - ii. If yes, how do you rate the new auditor's report format relative to the old format?
 - Same
 - Some improvement
 - Significant improvementComments?
 - iii. Do you think the inclusion of Key Audit Matters (KAMs) increase transparency about the audit performed?
 - Yes, most of the time
 - Yes, some of the time
 - NoComments?
 - iv. Do you consider that the inclusion of Key Audit Matters (KAMs) increases your confidence in the external audit process?
 - Yes, most of the time
 - Yes, some of the time
 - NoComments?
 - v. Do identified Key Audit Matters (KAMs) align with your concerns and provide better insights about key matters?
 - Yes, most of the time
 - Yes, some of the time
 - NoComments?

vi. In your experience, are the KAMs using entity specific, customised language?

- Yes, most of the time
- Yes, some of the time
- No

Comments?

vii. Can you provide example(s) of very useful auditor's reports that you have seen? What sets them apart from others?

viii. Auditors are not required to include conclusions or findings about KAMs but some auditors have opted to include this information. Have you seen KAMs with conclusions or findings included?

- Yes
- No

If yes, did you find the conclusions or findings about KAMs helpful?

- Yes, conclusions or findings about KAMs were helpful
- No, conclusions or findings about KAMs were not helpful

Comments

ix. Auditors are not required to disclose materiality but some auditors have opted to do so. Have you seen auditor reports where materiality levels are reported?

- Yes
- No

If yes, did you find the disclosure of materiality helpful?

- Yes, information about materiality is helpful
- No, information about materiality is not helpful

Comments

x. For future consideration in enhancing the auditor's report, please indicate by checking the items below or adding your own suggestions, which areas, that may not be included in auditor's reports currently but, that you believe would further improve transparency about the audit:

- More explicit evaluation of how aggressive or conservative the company's accounting practice is
- Benchmarks used by the auditor
- Materiality
- Internal control assessment
- More granular description of risks
- Audit work
- Audit findings
- More information on work done on significant risks
- Changes to the audit approach
- Risk assessment during the audit (versus what was planned)

- Changes from prior year
- Critical areas where professional judgement and assumptions have been addressed
- Assumptions made by management
- Other
- None

5. Does the Board have any feedback:

- 1. On the approach of asking the shareholders association to run a survey requesting feedback from its members to target investors response?**
- 2. On additional investors to target?**
- 3. On the questions posed?**

Target group: Those charged with governance

6. We have requested assistance from practitioners to identify clients that may be willing to share their experience of Key Audit Matters with the XRB. We are compiling a list of targets, noting that the June year end reporting season may be the ideal opportunity to identify good targets. We have approached the various firms to identify key clients that may be willing to discuss the experience with us. If Board members identify specific targets, we request that you identify these (and provide contact details) to staff.
 7. We plan to conduct one on one interviews (either through meetings or over the phone) to obtain an understanding of the experience to date during August.
 8. Alternatively, we could identify the head of the audit committee for each of the entities that have had a revised auditor's report issued and either send them a request to participate or request that the auditors extend the invitation for their client to participate in an online survey monkey (depending on whether you consider that the response rate will differ depending on who asks them to participate).
 9. Draft questions identified include:
 - 1) What is your role at your organisation?
 - 2) What involvement do you have with the auditors of your entity?
 - 3) What was the level of involvement in the auditor reporting process, given the requirement for the auditor to report Key Audit Matters?
 - o Minimal (i.e. read the report at the end of the audit)
 - o Moderate (i.e. discussion on description of KAMs in advance of finalising)
 - o Extensive (i.e. involved in discussions relating to identification of KAMs, adequacy of disclosures and description of KAMs)
 - 4) How does this compare to your previous involvement in the auditor reporting process?
 - 5) Given your involvement in the auditor's reporting process, do you consider that you now have a better understanding of the audit process and/or about significant issues considered by the auditors?
 - 6) Do you consider that the KAM requirements have had a positive impact on the robustness/timeliness of the discussions on key audit matters with the auditor?
 - 7) Do you consider that this has had a positive impact on audit quality?
 - 8) Did the discussions around KAM result in any changes to the annual report?
 - 9) Did you consider there was a need to respond to KAMs in the annual report?
 - 10) Have you had any feedback (positive or negative) from investors, at AGMs, or other sources on the changes to the auditor's report?
 - 11) Auditors are not required to include conclusions or findings about KAMs but some auditors have opted to include this information. Did your auditor include KAMs with conclusions or findings?
 - i. Yes
 - ii. No
- If yes, did you find the conclusions or findings about KAMs helpful?
- i. Yes, conclusions or findings about KAMs were helpful
 - ii. No, conclusions or findings about KAMs were not helpful

Comments

12) Auditors are not required to disclose materiality but some auditors have opted to include this information. Did your auditor include materiality in the auditor's report?

- i. Yes
- ii. No

If yes, did you find the disclosure about materiality levels helpful?

- iii. Yes, conclusions or findings about KAMs were helpful
- iv. No, conclusions or findings about KAMs were not helpful

Comments

13) Did you find that the language used by your auditor in reporting KAMs was specific to your company and the reporting period?

14) Did your audit fees increase as a result of the revised auditor reporting requirements?

15) Do you have any feedback on how the auditor reporting process could be improved?

16) For future consideration in enhancing the auditor's report, please indicate by checking the items below or adding your own suggestions, which areas, that may not be included in auditor's reports currently but, that you believe would further improve transparency about the audit:

- i. More explicit evaluation of how aggressive or conservative the company's accounting practice is
- ii. Benchmarks used by the auditor
- iii. Materiality
- iv. Internal control assessment
- v. More granular description of risks
- vi. Audit work
- vii. Audit findings
- viii. More information on work done on significant risks
- ix. Changes to the audit approach
- x. Risk assessment during the audit (versus what was planned)
- xi. Changes from prior year
- xii. Critical areas where professional judgement and assumptions have been addressed
- xiii. Assumptions made by management
- xiv. Other
- xv. None

10. Does the Board have any feedback:

- a. On the approach of asking practitioners to identify suitable candidates to approach?
- b. On additional candidates to target?
- c. On whether all entities that have had a KAM report should be invited to participate in a survey monkey?
- d. On the draft questions to raise with those charged with governance?

Target group: Practitioners

11. We consider that a survey monkey targeting the engagement partners that have been named in the revised auditor reports will be the most efficient way to target all practitioners. The FMA has been tracking and already has a list of engagement partners involved. In addition or alternatively, we can arrange smaller roundtables, and invite the technical person from each of the big 4 firms, responsible for the review and oversight of the revised auditor reports to attend sessions at the XRB offices. We will reach out to the mid-tier firms to determine appropriate partners to seek feedback from.
12. The following questions have been identified for practitioners:

Background and context

- 1) What type of firm/practice are you part of:
 - Big four
 - Mid-tier firm
 - Other
- 2) What is the total number of listed entity audit engagements you completed since the new auditor reporting requirements have come into effect?
- 3) Have you voluntarily reported KAMs on any engagements, or early adopted the reporting of KAM for any non-listed issuers?
If yes:
 - How many voluntary or early KAM reports have you prepared?
 - What were the drivers for voluntarily reporting KAM or early adopting the KAM reporting requirements?

Value and benefit of the revised report, including Key Audit Matters

- 4) What was the level of involvement in the auditor reporting process on average for the following stakeholders?
 - Management
 - Minimal (i.e. read the report at the end of the audit)
 - Moderate (i.e. discussion on description of KAMs in advance of finalising)
 - Extensive (i.e. involved in discussions relating to identification of KAMs, adequacy of disclosures and description of KAMs)
 - Audit Committee
 - Minimal (i.e. read the report at the end of the audit)
 - Moderate (i.e. discussion on description of KAMs in advance of finalising)
 - Extensive (i.e. involved in discussions relating to identification of KAMs, adequacy of disclosures and description of KAMs)

Comments

5) Did the KAM requirements have a positive impact on the robustness/timeliness of discussions with the client?

- Yes, for all engagements
- Yes, for most engagements
- Yes, for some engagements
- No

Comments

If yes, do you consider that this had a positive impact on audit quality?

- Yes, most of the time
- Yes, some of the time
- No

Comments

6) Did the discussions around Key Audit Matters result in any changes to:

a) The financial statements, including disclosures?

- Yes, for all engagements
- Yes, for most engagements
- Yes, for some engagements
- No

Comments/examples

b) The rest of the annual report, including disclosures outside of the financial statements (e.g., CEO statements, Audit committee reporting, etc.)?

- Yes, for all engagements
- Yes, for most engagements
- Yes, for some engagements
- No

Comments/examples

7) Did the KAM disclosures trigger any communications from investors?

- Yes, for all engagements
- Yes, for most engagements
- Yes, for some engagements
- No

Comments/description of the types of things raised in communications.

8) Have you received any feedback (positive or negative) from investors, at AGMs, or other sources on the changes to the auditor's report?

- Yes, for all engagements
- Yes, for most engagements
- Yes, for some engagements
- No

Comments

9) To what extent do you consider that the following are benefits from implementing the revised auditor reporting standards:

[For each option provide a 3-point scale: did not see a benefit/moderate benefit/significant benefit]

- Enhanced communication with clients
- Enhanced financial statement disclosure on key matters
- Opportunity to demonstrate the value of the audit
- Improved audit quality.

10) Do you believe there are cons to implementing the revised auditor reporting requirements?

- Yes
- No

If yes, are these cons:

- Increased costs, that cannot be passed on
- Perceived increase in liability
- Other

Comment
What can be done to address the drawbacks?

11) Do you consider that the benefits outweigh the costs of implementing the revised auditor reporting requirements?

- Strongly agree
- Agree
- Neutral
- Disagree
- Strongly disagree

Comments

Application of the new KAM requirements

12) Have you chosen to communicate “conclusions” or “findings” about KAMs?
[to tailor specific to firm]

- i. Yes, for all engagements
- ii. Yes, for most engagements
- iii. Yes, for some engagements
- iv. No

If you answered Yes:

If so, have any concerns been raised about their inclusion such as implied separate opinions or other unintended consequences, either within your firm, from management or those charged with governance, or from regulators?

- i. Yes, concerns have been raised for most engagements
- ii. Yes, concerns have been raised for some engagements
- iii. No concerns have been raised
- iv. The opposite, feedback received did not raise concern rather the feedback sought a “conclusion” or “finding”

Comment

If concerns have been raised about communicating a “conclusion” or “finding” about KAM, what were they?

Comment

If you have only chosen to communicate “conclusions” or “findings” about KAMs for some engagements, what are the drivers for including or excluding them?

Comment

13) Did you choose to communicate materiality and/or benchmarks used?
[to tailor specific to firm]

- i. Yes, for all engagements
- ii. Yes, for most engagements
- iii. Yes, for some engagements
- iv. No

Comment

If you have only chosen to communicate materiality for some engagements, what are the drivers for including or excluding this information?

Comment

If you have chosen not to communicate materiality what were the key drivers for excluding this information?

Comment

14) Are there aspects of the standard that are difficult to understand?

- Yes
- No

If yes, please specify

15) Are there aspects of the new or revised standards that are difficult to implement?

- Yes
- No

If yes, please specify

16) Have you had to issue a KAM report for the second year on any clients (i.e. for early adopters of the new requirements)?

[to tailor specific to firm]

- Yes
- No

If yes, how difficult was it to avoid issuing an auditor's report that was a copy of the prior year?

- It was relatively easy to tailor the report for the specific year under audit
- It required some thought, but the KAMs were tailored and specific to each period
- It was difficult to tailor the report year on year, as the matters and reasons for identifying a KAM remain the same

Comments

Costs

17) On average how many incremental hours were spent, in the first year of implementation of the revised standards, relating to KAMs?

[Question for the Board: Should this be a percentage of the total time?]

- 0-5 hours
- 5-10 hours
- 10-20 hours
- 20-30 hours
- 30-40 hours
- 40-50 hours
- >50 hours

What percentage of incremental time involved:

- Partner time
- Quality control reviewer
- Other senior level review
- Staff time

18) Of those additional hours, on average how much was recoverable from your clients?

- >80%
- Between 50% - 80%
- Between 25% - 50%
- Between 0% - 25%
- None

Please provide detail

19) For engagements where you have implemented the KAM requirements for a second year, did the average change in hours spent on discussing and drafting KAMs decrease, remain neutral, or increase?

- Average hours decreased in the 2nd year of implementation
- Average hours remained neutral
- Average hours decreased in the 2nd year of implementation

Comment.

Please indicate a percentage to illustrate the increase or decrease

Going forward, do you expect the average time spent on discussing and drafting KAMs to decrease, remain neutral, or increase?

- Average hours expected to decrease in the 2nd year of implementation
- Average hours expected to remain neutral
- Average hours expected to decrease in the 2nd year of implementation

Comment

Please indicate a percentage to illustrate the expected increase or decrease

Internal quality of enhanced report

20) Does your firm have standard wording for common KAMs that arise?

- Yes

1. Sliding scale response:

- a. We encourage practitioners to always include additional detail specific to their individual client
- b. Practitioners are encouraged to use standard wording to drive consistent quality across the firm

- No

Comments

21) Does your firm have a policy or practice to review KAMs across the client base for consistency by industry?

- Yes

1. Does the review occur:

- a. Pre-issuance
- b. Post-issuance
- c. Varies

- No

Comments

Lessons learned

22) As you and your firm become more familiar with the revised auditor reporting process, is there anything that you would do differently to improve the process?

- No
- Yes, on some engagements
- Yes, for all engagements

Comments

13. Does the Board have any feedback:

- a. **On the approach of targeting a representative from each of the big four and mid-tier firms to hold interviews with?**

- b. On whether all engagement partners who have signed new auditor reports should be invited to participate in a survey monkey?**
- c. On the draft questions to raise with practitioners?**

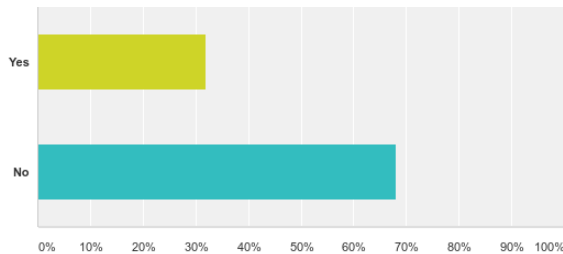


Feedback request for Investor's views on the new audit reports

June 2017

Q1: Have you had the opportunity to see the new audit report format yet?

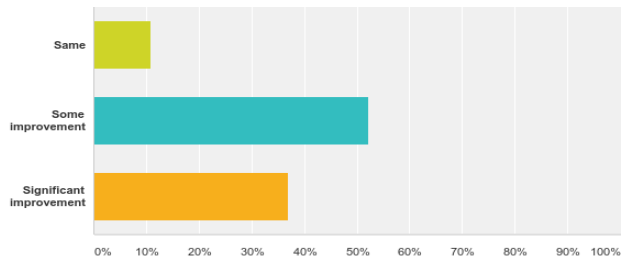
• Answered: 128 Skipped: 1



Answer Choices	Responses	
Yes	32.03%	41
No	67.97%	87
Total		128

Q2: If 'Yes', how do you rate the new audit report format relative to the old format?

• Answered: 46 Skipped: 83



Answer Choices	Responses	Count
Same	10.87%	5
Some improvement	52.17%	24
Significant improvement	36.96%	17
Total		46

3

Q2: If 'Yes', how do you rate the new audit report format relative to the old format?

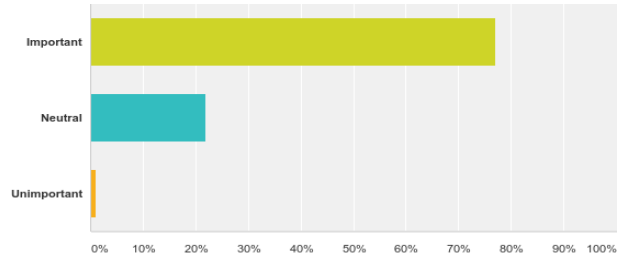
Comments:

- Very significant change which provides a better understanding of the audit process and greater confidence in the process and outcome.
- Does it say anything new or is it just new "duck for cover words?"
- I now have a better idea of the areas audited and the reasoning behind why these areas were audited.
- Actually, I think it is a step backward. The previous standard provided hardly any useful information, but at least it didn't require many forests to die. The new standard invites to writing novels which still don't contain a lot of useful information. Why not offering a meaningful scoreboard instead of endless pages full of boring repetitions?
- Relevant but long.
- I never read the audit report unless there is a reservation.
- Critical to identify issues that involve a judgement call by directors.
- Offers little if any additional value. How often do we see comments of concern from an auditor? I can't remember any.
- Saw ikeGPS -very impressed - esp. "Audit Scope" and KAM.
- It clarifies what the auditors actually did and thus provides some comfort that shareholders interests are being looked after.
- I was an auditor until very recently and did get exposure to the new report format before they became mandatory. I have read only one audit report so far, for Blis which was audited by Deloitte and I must admit it was a bit disappointing. Yes, the key audit matters are disclosed but Deloitte have been scrupulous about avoiding any opinion on anything except the normal opinion statement. Instead, the analysis of key audit matters merely states the procedures that Deloitte followed which will be of little interest or use for the majority of investors.
- The non-financial information disclosure is a "double negative", i.e. the audit review did not identify anything that was inconsistent - Why can't this be a positive statement that the non financial information in the Annual Report is consistent.
- The auditor's opinion is first after listing the documents to which it relates in stead of last. It's still pretty wordy and the typeface in the FPH report is very small and, on screen, seems more grey and black.

4

Q3: Do you think the inclusion of Key Audit Matters (KAM's) is:

- Answered: 100 Skipped: 29



Answer Choices	Responses
Important	77.00% 77
Neutral	22.00% 22
Unimportant	1.00% 1
Total	100

5

Q3: Do you think the inclusion of Key Audit Matters (KAM's) is:

Comments:

- Gives excellent insights into what really mattered through the audit process.
- Shareholders should be made aware of significant KAMs.
- Gives me more confidence in the audit process and financial results.
- For financial markets to thrive investors **MUST** have confidence and transparency in a public company's reporting and any steps the FMA and NZSHA take to force companies to be more transparent the better.
- Important, but get rid of all the unnecessary weasel words (example: EVO).
- Don't Know but probably YES, important.
- Better than "Emphasis of Matter".
- Precise and correct reporting is essential for reliable and trustworthy information.
- I like the idea in principle.
- It is too early to say what impact this will have. I understand the stated rationale and it may be helpful for small investors in particular to understand the auditors key focus areas from a financial reporting perspective in any given year, and to be able to ask questions arising from that. It will be interesting to see how auditors report any significant points of weakness or risk going forward in specific cases. We have not seen any of those appear yet. That will assist to ascertain whether this initiative will make a substantive difference/ improve behaviour or standards.
- Just more information without offering any tangible conclusions. Of little value.
- The downside is the wordiness of the new reports. I have doubts as to the number of people who read the old style, and the extra length might put people off the new style, but at least the new one is much more meaningful. Also, future extraordinary items like the company moving offshore and significant changes to the operation of the company to be part of the audit.
- The current format is not very helpful. If the new format is more informative then I support it.

6

Q3: *Do you think the inclusion of Key Audit Matters (KAM's) is:*

Comments continued:

- It does provide much more focus on audit "issues" but can create an unhealthy focus on just one aspect of the accounts.
- Essential. However shareholders need to be educated to actually read it; most wont.
- I searched two companies 'Investor' pages, off your list but cannot find references to KAM but I will look out for them.
- I say this as historically audit reports often have not alerted investors to a company's imminent demise- I doubt that has changed.
- From my perspective, the jury is still out. We have learned a bit more but it is of little value for an investor making an investment decision.
- Still query however how much more information the new opinion provides. Interestingly in the Xero Audit report EY do not comment on tax losses even though Xero Directors identify this as a "Critical Accounting Estimate".
- Such issues confronting companies tend not to have been given prominence in times past.
- I have not as yet seen a report. Key Audit Matters can be significant. However I would not want a qualification to be hidden away among KAMs. I will await sighting of the new format and I hope where there is a qualification that it is readily noticeable.
- The standard Audit Reports are too bland, so this feels like a good move.
- After seeing the debacle at Fletcher's (That I really believe was covered until the last possible moment) I don't trust a system that requires voluntary honesty from the directors and upper management !!!
- Undecided what the benefit will be until I see what is reported. e.g. will the Fletcher Auditor delve into why there are significant losses on two projects and explain them. They should and it may make for a long Audit report.

7

NZAuASB Board Meeting Summary Paper

AGENDA ITEM NO.	7.1
Meeting date:	26 July 2017
Subject:	IESBA's Proposed Application Material Relating to Professional Scepticism and Professional Judgement exposure draft
Date:	3 July 2017
Prepared By:	Peyman Momenan

<input checked="" type="checkbox"/> Action Required	<input type="checkbox"/> For Information Purposes Only
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Agenda Item Objectives

For the Board to:

- CONSIDER the IESBA's exposure draft *Proposed Application Material Relating to:*
 - Professional Skepticism- Linkage with the Fundamental Principles; and
 - Professional Judgment- Emphasis on Understanding Facts and Circumstances
- NOTE submissions received from New Zealand constituents;
- APPROVE a New Zealand response to the IESBA.

Background

1. The IESBA issued an exposure draft *Proposed Application Materials Relating to Professional Skepticism and Professional Judgement* in May 2017. A communique was issued in New Zealand seeking comments on these proposals by the 7th of July. The NZAuASB has received one submission in relation to this ED which is included as Agenda item 7.3.
2. The IESBA is seeking feedback by **25 July 2017**. However, the IESBA has agreed to extend the due date of the NZAuASB's submission to 27 July 2017, given the timing of the July meeting of the NZAuASB.
3. The proposed additions to Section 120, *the conceptual framework*, of the proposed restructured *Code of Ethics for Professional Accountants* (the Code) are very limited in their nature and scope. At present, the Code only refers to professional scepticism and professional judgment in relation to independence considerations for audits, reviews and other assurance engagements. The IESBA has a longer-term plan for how concepts of professional scepticism and professional judgement need to be addressed in the Code that is likely to go beyond this. The ED is an interim step, proposing application material to assist professional accountants in applying Section 120 of the Code (in considering independence) until such time that a more comprehensive project can be undertaken.
4. We received two submissions from New Zealand constituents in relation to this ED, from KPMG (see Agenda item 7.3) and Professor Karen Van Peurseem from Victoria University of Wellington. The submission received from Professor Van Peurseem is an academic article

about professional scepticism and professional judgement in their broadest sense and meaning and not related to the very limited changes proposed by the IESBA at this stage. Accordingly, we will consider the article in relation to the IESBA's and IAASB's future plans for professional scepticism and professional judgement, once those plans are issued for consultation.

Recommendations

5. We recommend that the Board:

- CONSIDER the exposure draft;
- APPROVE a New Zealand submission to IESBA.

Material Presented

Agenda item 7.1	Board Meeting Summary Paper
Agenda item 7.2	Draft submission for approval
Agenda item 7.3	Response from KPMG
Agenda item 7.4	IESBA Exposure draft – Proposed Application Material Relating to Professional Skepticism and Professional Judgment

27 July 2017

Ken Siong
Technical Director
International Ethics Standards Board for Accountants
545 Fifth Avenue, 14th Floor
New York, 10017
USA

Dear Ken,

IESBA Exposure Draft – Proposed Application Material Relating to Professional Skepticism and Professional Judgment

Thank you for the opportunity to comment on the IESBA exposure draft *Proposed Application Material Relating to Professional Skepticism and Professional Judgment*. We submit the feedback from the New Zealand Auditing and Assurance Standards Board (NZAuASB).

The External Reporting Board (XRB) is a Crown Entity responsible for developing and issuing accounting and auditing and assurance standards in New Zealand. The XRB's outcome goal is to contribute to the creation of dynamic and trusted markets through the establishment of an accounting and assurance framework that engenders confidence in New Zealand financial reporting, assists entities to compete internationally and enhances entities' accountability to stakeholders. The NZAuASB has been delegated responsibility by the XRB for developing and issuing auditing and assurance standards, including ethical standards for assurance practitioners.

Overall comment

The NZAuASB notes that the IESBA has further plans to elaborate on the relevance of professional scepticism to compliance with the fundamental principles in the longer term. The NZAuASB agrees with the IESBA that appropriately addressing professional scepticism in the Code involves considerations beyond the limited changes proposed in the ED and looks forward for future communications in relation to those plans.

In relation to the questions requested to be addressed by the ED, the NZAuASB supports the proposed additions to clarify what is already implicit in the Code, in relation to the linkage between professional scepticism and the Fundamental Principles, as well as the emphasis on understanding facts and circumstances in exercising professional judgement when applying the conceptual framework. We believe these additions will be helpful in applying the conceptual framework in Section 120 of the proposed restructured Code until the IESBA's comprehensive response for addressing professional scepticism in the Code is prepared and implemented.

In formulating this response, the NZAuASB sought input from New Zealand constituents.

Should you have any queries concerning our submission please contact either myself at the address details provided below or Sylvia van Dyk (sylvia.vandyk@xrb.govt.nz).

Yours sincerely,

Robert Buchanan

Chairman

Email: robert@buchananlaw.co.nz

DRAFT

Submission of the New Zealand Auditing and Assurance Standards Board

IESBA Exposure Draft *Proposed Application Material Relating to:*

- (a) *Professional Skepticism-Linkage with the Fundamental Principles; and*
- (b) *Professional Judgment- Emphasis on Understanding Facts and Circumstances*

Schedule of Responses to the IESBA's Specific Questions

Proposed Application Material Relating to Professional Skepticism (paragraph 120.13 A1)

1. **Do respondents agree that the proposed application material enhances the understandability of the conceptual framework in Section 120 of the proposed restructured Code?**

Response:

The NZAuASB agrees that the proposed application material in para 120.13 A1 relating to professional scepticism clarifies what is already implicit in the conceptual framework. However, the NZAuASB notes that this paragraph states that "... Compliance with the fundamental principles supports the exercise of such professional scepticism. ...". The NZAuASB is of the view that the fundamental principles are part of the essential attributes that underpin professional scepticism. Thus, compliance with the fundamental principles is a prerequisite for appropriate application and demonstration of professional scepticism by professional accountants. The NZAuASB believes that there is a stronger linkage between the fundamental principles and professional scepticism than what is suggested by the proposed para 120.13. Therefore, the NZAuASB recommends replacing the word "support" with "underpin".

2. **Do the examples in the proposed application material clearly describe how compliance with the fundamental principles of integrity, objectivity, and professional competence and due care support the exercise of professional skepticism in the context of an audit of financial statements? If not, why not?**

Response:

We believe that recognising the fundamental principles as essential attributes of professional scepticism (as explained under question 1 above) will also provide a better flow for the examples in the proposed application material. For instance, professional scepticism involves "being alert to conditions which may indicate possible misstatement due to error or fraud". Recognising such conditions and being alert to their indicators require professional competency and due care. A professional accountant without an appropriate level of knowledge and skill for a particular engagement is unlikely to be able to identify all of the relevant indicators for risk of material misstatement that are relevant to a particular client's financial statements. Thus, the fundamental principle of professional competence and due care is a significant facilitator of professional scepticism.

Similarly, maintaining a questioning mind depends on, among other things, the professional accountant's ability to appropriately counter bias, conflict of interest or the undue influence of others. For example, previous involvement with a client, might give rise to a risk of bias by the professional accountant. Compliance with the fundamental principle of objectivity enables the professional accountant to be aware of this bias and to address such risks of bias by taking additional steps to critically evaluate relevant evidence.

We also believe guidance which addresses assurance engagements other than audit engagements (e.g. reviews and other assurance engagements) would be more useful. This is because there is already sufficient guidance around the independence risks when performing audits.

Proposed Application Material Relating to Professional Judgment (paragraph 120.5 A1)

3. Do respondents agree that the proposed application material enhances the understandability of the conceptual framework in Section 120 of the proposed restructured Code?

Response:

The NZAuASB agrees that the proposed application material in para 120.5 A1 relating to professional judgement enhances the understandability of the conceptual framework in Section 120 of the proposed restructured Code.

The NZAuASB notes that the proposed application material emphasizes the importance of professional accountants obtaining a sufficient understanding of the facts and circumstances known to them when exercising professional judgement in applying the conceptual framework, but it neither explains why this is important nor does it provide any examples. The explanatory memorandum provides a very good explanation of why this is important in para 14 of the ED.

“... if a professional accountant were to accept information at “face value” without regard to whether it could lead the professional accountant to become associated with materially false or misleading information, it would constitute non-compliance with the fundamental principles, in particular, integrity and professional competence and due care...”

The NZAuASB suggests adding the above statement to the application material to clarify the reason why obtaining sufficient understanding of the facts and circumstances their implication is important when exercising professional judgement in applying the conceptual framework.

4. Do respondents agree that the proposed application material appropriately emphasizes the importance of professional accountants obtaining a sufficient understanding of the facts and circumstances known to them when exercising professional judgment in applying the conceptual framework? If not, why not?

Response:

We believe that the application material provides relevant guidance about application of professional judgement when obtaining understanding of the facts and circumstances known to the professional account and some examples of the risks involved.

Chief Executive
External Reporting Board
PO Box 11250
Manners Street Central
WELLINGTON 6142
email: submissions@xrb.govt.nz

Our ref KPMG submission -
Proposed Application
Material Relating to
Professional
Skepticism.docx

28 June 2017

Dear Sir

Proposed Application Material Relating to:

- (a) Professional Skepticism –Linkage with the Fundamental Principles; and**
- (b) Professional Judgment – Emphasis on Understanding Facts and Circumstances**

KPMG welcomes the opportunity to provide comments on the consultation paper issued in May. We have reviewed that paper, and our comments are set out below.

Proposed Application Material Relating to Professional Skepticism (paragraph 120.13 A1)

- 1 Do respondents agree that the proposed application material enhances the understandability of the conceptual framework in Section 120 of the proposed restructured Code?**

We believe it has.

- 2 Do the examples in the proposed application material clearly describe how compliance with the fundamental principles of integrity, objectivity, and professional competence and due care support the exercise of professional skepticism in the context of an audit of financial statements? If not, why not?**

Whilst we believe the examples given are clear and provide some good guidance, we believe guidance which addresses the other engagements (review and assurance) would be more useful. This is because there is already sufficient guidance around the independence risks when performing audits.

Proposed Application Material Relating to Professional Judgment (paragraph 120.5 A1)

- 3 Do respondents agree that the proposed application material enhances the understandability of the conceptual framework in Section 120 of the proposed restructured Code?**

We believe it has.

- 4 Do respondents agree that the proposed application material appropriately emphasizes the importance of professional accountants obtaining a sufficient understanding of the facts and circumstances known to them when exercising professional judgment in applying the conceptual framework? If not, why not?**

We believe the application material provides some valuable guidance around when professional judgement should be exercised and some of the risks that need to be considered.

Yours faithfully



Darby A Healey
Partner

Exposure Draft

May 2017

Comments due: July 25, 2017

*International Ethics Standards Board
for Accountants®*

Proposed Application Material Relating to:

- (a) Professional Skepticism –
Linkage with the
Fundamental Principles; and
- (b) Professional Judgment –
Emphasis on Understanding
Facts and Circumstances



International
Ethics Standards
Board for Accountants®

This Exposure Draft was developed and approved by the International Ethics Standards Board for Accountants® (IESBA®).

The IESBA is a global independent standard-setting board. Its objective is to serve the public interest by setting high-quality ethics standards for professional accountants worldwide and by facilitating the convergence of international and national ethics standards, including auditor independence requirements, through the development of a robust, internationally appropriate *Code of Ethics for Professional Accountants™* (the Code).

The structures and processes that support the operations of the IESBA are facilitated by the International Federation of Accountants® (IFAC®).

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REQUEST FOR COMMENTS

The proposals in this Exposure Draft may be modified in light of comments received before being issued in final form. Comments are requested by **July 25, 2017**.

Respondents are asked to submit their comments electronically through the IESBA website, using the "[Submit a Comment](#)" link. Please submit comments in both PDF and Word files. Also, please note that first-time users must register to use this feature. All comments will be considered a matter of public record and will ultimately be posted on the website. Although the IESBA prefers that comments are submitted via its website, comments can also be sent to Ken Siong, IESBA Technical Director at KenSiong@ethicsboard.org

This publication may be downloaded from the IESBA website: www.ifac.org/ethics/restructured-code. The approved text is published in the English language.

PROPOSED APPLICATION MATERIAL RELATING TO PROFESSIONAL SKEPTICISM AND PROFESSIONAL JUDGMENT

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EXPLANATORY MEMORANDUM

I. Introduction

1. This memorandum provides background to, and an explanation of, the IESBA's exposure draft which includes proposed new application material to:
 - (a) Describe how compliance with the fundamental principles in the Code supports the exercise of professional skepticism in the context of audit and other assurance engagements; and
 - (b) Emphasize the importance of professional accountants obtaining a sufficient understanding of the facts and circumstances known to them when exercising professional judgment in applying the conceptual framework.

The application material represents proposed additions to Section 120¹ of the restructured Code, the text of which was [agreed in principle](#) by IESBA in December 2016 as part of Phase 1 of its Safeguards project.²

2. The IESBA approved this exposure draft in April 2017.

II. Significant Matters

A. Proposed Application Material Relating to Professional Skepticism – Linkage with the Fundamental Principles

Background

3. Professional skepticism is an important concept that is currently defined in auditing and assurance standards. The International Auditing and Assurance Standards Board's (IAASB's) International Standard on Auditing (ISA) 200, for example, defines professional skepticism as "an attitude that includes a questioning mind, being alert to conditions which may indicate possible misstatement due to error or fraud, and a critical assessment of audit evidence."³ ISAs, in particular, explicitly require auditors to exercise professional skepticism throughout the audit, i.e., during engagement acceptance; as part of identifying and assessing risks of material misstatement; in designing the nature, timing and extent of audit procedures; and in forming an opinion on whether the financial statements are prepared in all material respects in accordance with the applicable financial reporting framework. Although, the definition of professional skepticism in the auditing and assurance standards of national standard setters might differ slightly from how the term is defined in the International Standards of the IAASB, the general principles are the same.

¹ Section 120, *The Conceptual Framework*

² In December 2016, the IESBA completed the first phase of its Safeguards project aimed at improving the clarity, appropriateness, and effectiveness of the safeguards in the Code. For further information about this project, including how the IESBA is coordinating it with its Structure project aimed at enhancing the understandability and usability of the Code, and anticipated timelines, see the January 2017 [IESBA Update](#).

³ ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*, paragraph 13(l). IAASB Staff Publication, [Staff Questions and Answers – Professional Skepticism in an Audit of Financial Statements](#) issued in February 2012, further discusses considerations in the ISAs and International Standard on Quality Control (ISQC) 1, *Quality Control for Firms that Perform Audit and Reviews of Financial Statements, and Other Assurance and Related Services Engagement* that are relevant to the proper understanding and application of professional skepticism during an audit of financial statements.

EXPLANATORY MEMORANDUM

4. Although the concept of professional skepticism is most prominently dealt with in auditing and assurance standards, professional skepticism is also referred to in the Code⁴ and in the International Education Standards (IESs).⁵ Consistent with the International Standards of the IAASB, the extant Code refers to professional skepticism in the context of audit and other assurance engagements only.
5. In recent years, issues relating to professional skepticism have been cited by various stakeholders. For example, since 2012 International Forum of Independent Audit Regulators' (IFIAR's) has consistently identified professional skepticism as a finding in its global survey of audit inspection reports, in particular in relation to the audit of areas that require high levels of professional judgment.⁶ At the national level, some jurisdictions have undertaken initiatives related to enhancing auditors' application of professional skepticism. The IAASB's December 2015 Invitation to Comment (ITC), [*Enhancing Audit Quality in the Public Interest: A Focus on Professional Skepticism, Quality Control and Group Audits*](#), summarized issues related to professional skepticism and sought views about how those issues might be addressed.⁷

⁴ The Code in particular refers to professional skepticism in its definition of independence:

Independence comprises:

(a) Independence of Mind

The state of mind that permits the expression of a conclusion without being affected by influences that compromise professional judgment, thereby allowing an individual to act with integrity and exercise objectivity and professional skepticism.

(b) Independence in Appearance

The avoidance of facts and circumstances that are so significant that a reasonable and informed third party would be likely to conclude, weighing all the specific facts and circumstances, that a firm's, or a member of the audit team's, integrity, objectivity or professional skepticism has been compromised. [*Emphases added*]

⁵ References to professional skepticism in the standards of the International Accounting Education Standards Board (IAESB) include the following:

- Applicable to all professional accountants, IES 3, *Initial Professional Development – Professional Skills* (2015), paragraph 7(c)(ii) includes as a learning outcome for professional skills the need to “apply professional skepticism through questioning and critically assessing all information.”
- Applicable to all professional accountants, IES 4, *Initial Professional Development – Professional Values, Ethics and Attitudes*, paragraph 11(a)(i) includes as a competency area for professional values, ethics and attitudes “professional skepticism and professional judgment.” It also describes related learning outcomes as follows:
 - “Apply a questioning mindset critically to assess financial information and other relevant data; and
 - Identify and evaluate reasonable alternatives to reach well-reasoned conclusions based on all relevant facts and circumstances.”
- Applicable to audit engagement partners only, IES 8, *Professional Competence for Engagement Partners Responsible for Audits of Financial Statements* prescribes learning outcomes for professional skepticism and professional judgment that engagement partners are expected to develop and maintain through continuing professional development.

Separately, reference is made to the term “skepticism” in a July 2015 non-authoritative IAESB publication titled, [*Framework for International Education Standards for Professional Accountants and Aspiring Professional Accountants*](#) (the Framework). Paragraph 28 of the Framework notes that “General education helps professional accountants and aspiring professional accountants integrate technical competence, professional skills, and professional values, ethics, and attitudes developed through professional accounting education. It supports the development of decision making skills, judgment, and skepticism.”

⁶ See the IFIAR Reports on Survey of Inspection Findings for 2012-2016. For example, in its 2016 Report dated March 2017, IFIAR highlights its continued focus on encouraging the development of standards that drive auditors to consistently exercise sufficient professional skepticism.

⁷ The IAESB considered the significant matters raised by respondents to the ITC at its [September 2016 meeting](#).

6. Additionally, some stakeholders, in commenting on recent IESBA exposure drafts,⁸ have suggested that the IESBA consider how the Code should address professional skepticism beyond audit and other assurance engagements. As further discussed in the Appendix to this explanatory memorandum, those stakeholders have expressed the view that the concept of professional skepticism should be relevant to all professional accountants – not just professional accountants who perform audit and other assurance engagements.
7. In response, the IESBA, IAASB and the IAESB jointly established a tripartite Professional Skepticism Working Group (PSWG) in June 2015. The PSWG's subsequent work prompted focused and coordinated discussions at the plenary sessions of the IESBA, IAASB, IAESB and their respective Consultative Advisory Groups (CAGs) about actions that the three Boards could take, individually and in coordination, to enhance the exercise of professional skepticism.
8. In September 2016, the PSWG recommended that the IESBA provide guidance in the Code to professional accountants undertaking audit, review and other assurance engagements to explain how compliance with the fundamental principles supports the exercise of professional skepticism in the context of such engagements.
9. This recommendation is consistent with the advice from the joint CAGs of the IESBA and IAASB. It was also based on feedback from some respondents to the IAASB's ITC and a [December 2015 summary of academic research](#) relating to professional skepticism that the IAASB had commissioned, which suggested that proper application of, and compliance with, the provisions in the Code might also contribute to enhancing the exercise of professional skepticism. Consistent with the PSWG's observations, the academic research notes that :
 - (a) The drivers and impediments to compliance with the fundamental principles and to the exercise of professional skepticism are the same.
 - (b) Auditors who comply with the fundamental principles (in particular integrity, objectivity and professional competence and due care) are more resolute when making inquiries of and considering evidence received from management.
 - (c) Substantial time pressure, particularly at year end, which creates threats to compliance with the fundamental principles, also impairs an individual's ability to exercise professional skepticism.

The IESBA's Response

10. In response to the PSWG's recommendation and recognizing the public interest in promoting the application of professional skepticism in audits, reviews and other assurance engagements, the IESBA determined that it would be important to supplement the Code's existing few references to professional skepticism with application material.
11. The proposed application material in paragraph 120.13 A1 explains how compliance with the fundamental principles supports the exercise of professional skepticism by illustrating this linkage in the context of an audit of financial statements.

⁸ August 2014 Exposure Draft, [Proposed Changes to Certain Provisions of the Code Addressing the Long Association of Personnel with an Audit or Assurance Client](#); and November 2014 Exposure Draft, [Proposed Changes to Part C of the Code Addressing Presentation of Information and Pressure to Breach the Fundamental Principles](#)

12. The IESBA is of the view that further work is needed in the longer term to elaborate on the relevance of professional skepticism to compliance with the fundamental principles. As further discussed in the Appendix to this explanatory memorandum, the IESBA has been considering whether and, if so, how the Code should address the applicability of the concept of professional skepticism to professional accountants other than professional accountants who perform audit and other assurance engagements.
13. Notwithstanding its plans for future work on the topic of professional skepticism, the IESBA determined that it should not withhold an immediate response to specific requests for clarification about how compliance with the fundamental principles supports the exercise of professional skepticism in the audit and assurance context.

B. Proposed Application Material Relating to Professional Judgment – Emphasis on Understanding Facts and Circumstances

Background

14. Concurrently with its deliberation of the issues relating to professional skepticism and its work on the Structure and Safeguards projects, the IESBA considered the views of stakeholders who questioned whether the relevant information underpinning ethical decisions is being assessed with sufficient rigor. The IESBA determined that if a professional accountant were to accept information at “face value” without regard to whether it could lead the professional accountant to become associated with materially false or misleading information, it would constitute non-compliance with the fundamental principles, in particular, integrity and professional competence and due care.
15. On that basis, the IESBA explored establishing a new requirement in the Code for professional accountants to apply a critical mindset when applying the conceptual framework in order to emphasize the need for professional accountants to understand facts and circumstances being considered and their implications with respect to compliance with the fundamental principles. Subsequent discussions with the IAASB highlighted the potential for confusion between the concepts of “critical mindset” and professional skepticism, given the overlapping aspect of critical assessment common to both concepts. The IESBA also considered whether it was necessary to introduce a new requirement as part of the application of the conceptual framework, or whether the notion of obtaining a sufficient understanding of the facts and circumstances was not already an implicit part of the requirement to exercise professional judgment when applying the conceptual framework. Against this background, the IESBA determined to pursue an alternative approach of developing application material focused on emphasizing the importance of professional accountants obtaining a sufficient understanding of the facts and circumstances known to the professional accountant when exercising professional judgment in applying the conceptual framework.

Proposed Application Material Relating to the Requirement to Exercise Professional Judgment When Applying the Conceptual Framework

16. In light of the above, the IESBA proposes application material in paragraph 120.5 A1 that emphasizes the importance of professional accountants obtaining a sufficient understanding of the facts and circumstances known to them when exercising professional judgment in applying the conceptual framework. Specifically, this proposed application material highlights the importance of the professional accountant considering whether:
 - There is an inconsistency between the known facts and circumstances and the professional accountant’s expectations.

- The information provides a reasonable basis on which to reach a conclusion.
 - Other reasonable conclusions could be drawn from the information being considered.
 - The professional accountant's own preconception or bias might be affecting the professional accountant's judgment.
 - The professional accountant's own expertise and experience are sufficient, or whether there is a need to consult with others with relevant expertise or experience.
17. The proposed application material is aligned to the discussion of professional judgment in the IAASB's standards.⁹
18. The IESBA believes that the proposed application material is a meaningful addition to the proposed restructured Code because it makes explicit an expectation that the IESBA believes is already implicit in the application of the conceptual framework. Therefore, the IESBA determined that it would be in the public interest to make this proposed application material available as part of the restructured Code when it is issued.

III. Analysis of Overall Impact of the Proposed Changes

19. The IESBA believes that the proposed application material in paragraphs 120.5 A1 and 120.13 A1 relating to professional judgment and professional skepticism, respectively, will clarify what is already implicit in the provisions of the Code. Consequently, it is not expected that the proposals will introduce any significant additional costs for professional accountants already complying with the Code.
20. With respect to the proposed application material relating to professional skepticism, the proposed clarification will heighten auditors' focus on the provisions in the Code that are relevant to acting in a manner that supports the exercise of professional skepticism. Consequently, the IESBA believes that the proposed application material in 120.13 A1 will contribute to improving audit quality.

IV. Project Timetable and Effective Date

21. The IESBA intends to finalize the proposed application material at the same time as its Structure project by December 2017. It also proposes to align the effective date of the proposed application material with the effective date of the restructured Code (see January 2017 [IESBA Update](#)).

V. Guide for Respondents

22. The IESBA welcomes comments on all matters addressed in this exposure draft, but especially those identified in the Request for Specific Comments below. Comments are most helpful when they refer to specific paragraphs, include the reasons for the comments, and, where appropriate, make specific suggestions for any proposed changes to wording. When a respondent agrees with proposals in this Exposure Draft, it will be helpful for the IESBA to be made aware of this view.

⁹ See ISA 200, paragraphs 13(k), 16 and A23–A27. The IAASB's standards define *professional judgment* as "the application of relevant training, knowledge and experience, within the context provided by auditing, accounting, and ethical standards, in making informed decisions about the courses of action that are appropriate in the circumstances of the audit engagement."

Request for Specific Comments

Proposed Application Material Relating to Professional Skepticism (paragraph 120.13 A1)

1. Do respondents agree that the proposed application material enhances the understandability of the conceptual framework in Section 120 of the proposed restructured Code?
2. Do the examples in the proposed application material clearly describe how compliance with the fundamental principles of integrity, objectivity, and professional competence and due care support the exercise of professional skepticism in the context of an audit of financial statements? If not, why not?

Proposed Application Material Relating to Professional Judgment (paragraph 120.5 A1)

3. Do respondents agree that the proposed application material enhances the understandability of the conceptual framework in Section 120 of the proposed restructured Code?
4. Do respondents agree that the proposed application material appropriately emphasizes the importance of professional accountants obtaining a sufficient understanding of the facts and circumstances known to them when exercising professional judgment in applying the conceptual framework? If not, why not?

Request for General Comments

23. In addition to the request for specific comments above, the IESBA is also seeking comments on the matters set out below:
 - (a) *Small and Medium Practices (SMPs)* – The IESBA invites comments regarding any aspect of the proposals from SMPs.
 - (b) *Regulators and Audit Oversight Bodies* – The IESBA invites comments on the proposals from an enforcement perspective from members of the regulatory and audit oversight communities.
 - (c) *Developing Nations* – Recognizing that many developing nations have adopted or are in the process of adopting the Code, the IESBA invites respondents from these nations to comment on the proposals, and in particular on any foreseeable difficulties in applying them in their environment.
 - (d) *Translations* – Recognizing that many respondents may intend to translate the final changes for adoption in their own environments, the IESBA welcomes comment on potential translation issues respondents may note in reviewing the proposals.

Matters Relating to the Applicability of Professional Skepticism Beyond the Audit and Assurance Context— Background and Future Considerations¹⁰

Calls for Extending the Applicability of Professional Skepticism to All Professional Accountants

1. As explained in paragraph 6, some stakeholders have suggested that the IESBA consider how the Code should address professional skepticism beyond audit and other assurance engagements. Those stakeholders have expressed the view that the concept of professional skepticism should be relevant to all professional accountants – not just professional accountants who perform audit and other assurance engagements. For example:
 - In its April 2015 [comment letter](#) to the IESBA, the International Organization of Securities Commissions (IOSCO) called on the IESBA to emphasize in the Code the need for professional accountants in business (PAIBs) to exercise an adequate level of professional skepticism throughout the process of preparing, presenting and/or filing information. IOSCO noted that:
 - PAIBs' work typically involves accumulating, distilling, and interpreting information from others, namely colleagues who work at the source (e.g., in operating departments) of an entity's transactions.
 - Given the increased level of complexity of business transactions and financial reporting and the increasing use of estimates and management judgments, PAIBs should be required to demonstrate enhanced levels of attentiveness and sensitivity to the integrity of information with which they are associated.
 - Participants in a 2014 Public Interest Oversight Board (PIOB) Public Interest Workshop suggested that “professional skepticism as a state of the mind and attitude should govern the performance of auditors, and inspire the attitude of other accountants, e.g., accountants in business.” They further noted that “when accountants (practitioners, non-practitioners, accountants in business) do not display proper professional skepticism it is recognized as a barrier to effective performance.”¹¹
 - Representatives of the PIOB at the March 2017 IESBA and IESBA CAG meetings expressed the view that the concept of professional skepticism is relevant to all professional accountants and that it is in the public interest that guidance on professional skepticism be made available to all professional accountants.

Issues, IESBA Deliberations and Decisions

2. Concurrently with its deliberations on developing the proposed application material in paragraph 120.13 A1, the IESBA has been considering whether and, if so, how the Code should address the applicability of the concept of professional skepticism to professional accountants other than professional accountants who perform audit and other assurance engagements.

¹⁰ The IESBA is not seeking comments on the matters outlined in this Appendix at this time.

¹¹ See [Conclusions from the PIOB Public Interest Workshop](#).

3. The IESBA noted that:
 - Professional skepticism is defined in the IAASB's International Standards and, as a concept, is long established in audit and assurance literature, with a very specific and clearly defined meaning in the context of audit and other assurance engagements.
 - The IAESB' standards already require professional skepticism to be a competency area for professional values, ethics and attitudes that all professional accountants should have. As stated in footnote 5, the IAESB's standards require all professional accountants to "apply a questioning mindset critically to assess financial information and other relevant data;" and "Identify and evaluate reasonable alternatives to reach well-reasoned conclusions based on all relevant facts and circumstances."
4. The IESBA's preliminary discussions with the IAASB and the joint CAGs of the IESBA and IAASB have identified a number of concerns about a potential for dilution of the meaning and importance of professional skepticism in the audit and assurance context if its applicability were to be extended beyond audit and assurance. Other concerns raised included, among others:
 - A potential need to reconsider the definition of professional skepticism in the IAASB's International Standards and the implications that might have for the nature and extent of auditors' and assurance practitioners' work effort; and
 - Potential implications for the nature and extent of work effort related to the provision of other types of professional services by professional accountants in public practice, for example, financial statement compilations and tax return preparation.

Also, the IESBA recognizes that broadening the applicability of professional skepticism to all professional accountants could create implications for how the IAESB's standards address professional skepticism.

5. In regard to the above, the IESBA notes that:
 - The IAASB's future considerations include analyzing potential fundamental changes to the concept and definition of professional skepticism in its International Standards.
 - The IAESB's extant standards use the IAASB's definition of professional skepticism and that the IAESB is planning to explore whether there is a need for clarification about professional skepticism in its standards.
6. Given the complexities described above and the desirability of a coordinated approach with ongoing initiatives by the IAASB and the IAESB, the IESBA intends to consider whether and, if so, how to extend the concept of professional skepticism to all professional accountants. This will involve consulting with stakeholders on relevant matters, including:
 - The implications of extending the concept of professional skepticism to all professional accountants (including those matters identified above).
 - Whether the Code should include more guidance on how to overcome impediments to the exercise of professional skepticism. Development of such guidance might include, for example, a consideration of:
 - Whether the limited references to bias in the Code might need to be further developed, leveraging relevant academic research on the topic.
 - Whether more application material is needed to explain how professional accountants

EXPLANATORY MEMORANDUM

should respond to external factors such as pressure.

- Whether the Code should describe the attributes that have been identified as drivers to the application of professional skepticism (e.g., “courage/fortitude”, critical thinking).
- Whether there is, in the public interest, a need to develop material to describe the role and expectations of professional accountants and how their work contributes to enhancing the integrity and credibility of information with which they are associated.

EXPOSURE DRAFT: PROPOSED APPLICATION MATERIAL RELATING TO (A) PROFESSIONAL SKEPTICISM – LINKAGE WITH THE FUNDAMENTAL PRINCIPLES; AND (B) PROFESSIONAL JUDGMENT – EMPHASIS ON UNDERSTANDING FACTS AND CIRCUMSTANCES

The IESBA's proposals include two sets of proposed application material presented in gray text below. The application material is a proposed addition to Section 120, *The Conceptual Framework* of the restructured Code.

A. Proposed New Application Material to Explain How Compliance with the Fundamental Principles Supports the Exercise of Professional Skepticism

Part 1 – COMPLYING WITH THE CODE, FUNDAMENTAL PRINCIPLES AND THE CONCEPTUAL FRAMEWORK

Section 120

The Conceptual Framework

...

Requirements and Application Material

...

Considerations for Audits, Reviews and Other Assurance Engagements

Independence

120.12 A1 Professional accountants in public practice are required to be independent when performing audits, reviews, or other assurance engagements. Independence is linked to the fundamental principles of objectivity and integrity. It comprises:

- (a) Independence of mind – the state of mind that permits the expression of a conclusion without being affected by influences that compromise professional judgment, thereby allowing an individual to act with integrity, and exercise objectivity and professional skepticism.
- (b) Independence in appearance – the avoidance of facts and circumstances that are so significant that a reasonable and informed third party would be likely to conclude that a firm's or an audit or assurance team member's integrity, objectivity or professional skepticism has been compromised.

120.12 A2 Parts 4A and 4B of the Code comprise the *International Independence Standards*. Parts 4A and 4B set out requirements and application material on how to apply the conceptual framework to maintain independence when performing audits, reviews or other assurance engagements. Professional accountants and firms are required to comply with these standards in order to be independent, when conducting such engagements. The conceptual framework to identify, evaluate and address threats to compliance with the fundamental principles applies in the same way to compliance with independence requirements. The categories of threats to compliance with the fundamental principles described in paragraph 120.6 A3 are also the categories of threats to compliance with independence.

Professional Skepticism

120.13 A1 Auditing, review and other assurance standards, including those issued by the International Auditing and Assurance Standards Board (IAASB), require professional accountants in public practice to exercise professional skepticism when planning and performing audits, reviews and other assurance engagements. Compliance with the fundamental principles supports the exercise of such professional skepticism. For example, in an audit of financial statements, this is illustrated in the following examples:

- *Integrity* requires the professional accountant to be straightforward and honest. Therefore, integrity supports the exercise of professional skepticism when the accountant is aware of or suspects that a position advanced by a client could result in financial statements being materially false or misleading. Being straightforward when raising concerns, pursuing inquiries or seeking further evidence before reaching a conclusion about a matter of concern is consistent with a questioning mind and the critical assessment of audit evidence involved in exercising professional skepticism.
- *Objectivity* requires the professional accountant to recognize that previous involvement with a client, among other things, might give rise to a risk of bias by the accountant. Self-awareness of the accountant's own bias when considering evidence relating to a matter material to the audit of the client's financial statements and taking additional steps to evaluate relevant evidence to address such risks of bias are actions consistent with exercising professional skepticism.
- *Professional competence and due care* requires the professional accountant to have the appropriate level of professional knowledge and skill required for a particular engagement, and to act diligently in accordance with applicable standards, laws and regulations. These attributes enable the accountant to identify risks of misstatement that are relevant to a particular client's financial statements and to exercise professional skepticism by diligently pursuing and then critically assessing whether audit evidence is sufficient and appropriate in the circumstances.

B. Proposed New Application Material to Emphasize the Importance of Understanding Facts and Circumstances in Relation to Exercising Professional Judgment

Part 1 – Complying with the Code, Fundamental Principles and the Conceptual Framework

...

Section 120

The Conceptual Framework

...

Requirements and Application Material

...

R120.5 When applying the conceptual framework, the professional accountant shall:

- (a) Exercise professional judgment;
- (b) Remain alert for new information and to changes in facts and circumstances; and
- (c) Use the reasonable and informed third party test as described in paragraph 120.6 A1.

Exercise of Professional Judgment

120.5 A1 Professional judgment involves the application of training, knowledge and experience taking into account the nature and scope of the professional activity being undertaken. When exercising professional judgment it is important that the professional accountant obtains a sufficient understanding of the facts and circumstances known to the accountant to identify, evaluate and address threats to compliance with the fundamental principles. In obtaining this understanding, the accountant might consider, among other matters, whether:

- There is an inconsistency between the known facts and circumstances and the accountant's expectations.
- The information provides a reasonable basis on which to reach a conclusion.
- Other reasonable conclusions could be drawn from the information being considered.
- The accountant's own preconception or bias might be affecting the accountant's judgment.
- The accountant's own expertise and experience are sufficient, or whether there is a need to consult with others with relevant expertise or experience.

Reasonable and Informed Third Party

120.5 A2A1 The reasonable and informed third party test is a consideration by the professional accountant about whether the same conclusions would likely be reached by another party. Such consideration is made from the perspective of a reasonable

EXPOSURE DRAFT

and informed third party, who weighs all the relevant facts and circumstances that the accountant knows, or could reasonably be expected to know, at the time the conclusions are made. The reasonable and informed third party does not need to be an accountant, but would possess the relevant knowledge and experience, to understand and evaluate the appropriateness of the accountant's conclusions in an impartial manner.

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NZAuASB Board Meeting Summary Paper

AGENDA ITEM NO.	8.1
Meeting date:	26 July 2017
Subject:	Long Association – Frequently Asked Questions (FAQs)
Date:	19 June 2017
Prepared by:	Misha Pieters

Action Required

For Information Purposes Only

Agenda Item Objectives

To:

- APPROVE New Zealand FAQs for the XRB website.

Background

1. Staff from the International Ethics Standards Board for Accountants (IESBA) have issued a series of FAQs to assist in the implementation of the revised long association provisions. These FAQs explain important aspects of the revised standard, including additional guidance relevant to the effective date and how the requirements apply to group scenarios.
2. We consider that these FAQs are important for New Zealand practitioners to read to ensure that the international provisions, when adopted in New Zealand, are appropriately applied.
3. The NZAuASB has exposed ED 2017-1 with the submission period closing at the end of July, proposing to adopt the revised long association provisions in New Zealand. IESBA staff have acknowledged that the FAQs may need to be amended when the restructuring project is complete. In addition, there may be additional New Zealand FAQs to add, once the New Zealand standard is finalised. We will monitor questions arising from the webinar, and submissions received to determine whether additional FAQs would be of assistance.
4. However, in the interim, we recommend issuing the FAQs, based on the IESBA staff FAQs, on the XRB website to assist practitioners as they consider the implications of the proposed changes to PES 1 (Revised).

Matters arising

5. We request feedback on the following matters:

- one additional New Zealand FAQ, relating to the definition of a public interest entity in New Zealand;
- whether the New Zealand FAQs should cover the IESBA staff wording relating to jurisdictions where a shorter cooling off period may apply in the interim; and
- the impact of the New Zealand Code referring to FMC reporting entity considered to have a higher level of public accountability rather than a listed entity related to the description of a related entity.

Action

6. We request that the Board:

- Approve the draft FAQs;
- Confirm the method of presentation – in a PDF document or more interactive FAQs, similar to the auditor reporting FAQs.

Material Presented

Agenda item 8.1	Board Meeting Summary Paper
Agenda item 8.2	Draft New Zealand FAQs
Agenda item 8.3	IESBA staff FAQs

Long Association FAQs

Introduction

The NZAuASB is proposing to amend the long association provisions in PES 1 (Revised) in line with changes finalised by the International Ethics Standards Board for Accountants (IESBA). These proposals amend the general provisions but will have the biggest impact for the audit of a public interest entity (PIE). Refer to ED NZAuASB 2017-1 for more detail about why the requirements are changing and what are the most significant changes.

Note

The IESBA is currently restructuring the revised long association provisions in accordance with the new structure and drafting conventions of the Code. The restructuring will not change the substance of the provisions. The restructured provisions are expected to be published as part of a restructured Code during 2018. These Q&As will be updated to align with the final restructured provisions when the restructured Code is issued.

These Frequently Asked Questions (FAQs) are intended to assist firms and other stakeholders adopt and implement the proposed revised long association provisions to be included within PES 1 (Revised) Code of Ethics for Assurance Practitioners. These FAQs highlight, illustrate or explain aspects of the revised partner rotation regime, and thereby assist in their proper application. These FAQs do not create new requirements, amend or override the Code.

** Acknowledgement*

Information in these FAQs has been drawn from the Frequently Asked Questions prepared by the staff of the International Ethics Standards Board for Accountants.

Public Interest Entity

Q:1. Which entities are considered to be public interest entities in New Zealand?

Commented [MP1]: New Zealand specific – drawn from ITC

A: PES 1 (Revised) defines a public interest entity as:

Any entity that is required or elects to prepare financial statements to comply with Tier 1 for-profit accounting requirements or Tier 1 PBE Accounting requirements in accordance with XRB A1.

The following table provides a snapshot of how the NZAuASB has analysed the types of entities that are PIEs in New Zealand:

Tier 1 For Profit Accounting Requirements				Tier 1 PBE Accounting Requirements		
Listed issuers	Other FMC reporting entities considered to have a higher	Large for-profit public sector entity	May opt down, but voluntarily applies tier 1	Large public sector entity	Large not-for profit entity	Other FMC reporting entities considered to have a higher level of public accountability

	level of public accountability ¹					
Both listed debt and equity	For example: <ul style="list-style-type: none"> Registered banks Insurers Credit unions Building societies Licensed derivative issuers Licensed MIS managers Recipients of money from a conduit issuer 	For example: <ul style="list-style-type: none"> Port companies Energy companies Airports State owned enterprise and Mixed ownership companies 		For example: <ul style="list-style-type: none"> Large DHBs Large government departments Large crown agents Large city /district/ regional councils Crown tertiary education institutions 	For example large registered charities	

Audit Partner Rotation Provisions

Q:2. In respect of an audit of a public interest entity (PIE), are all key audit partners subject to the same time-on and cooling-off periods?

A: The same maximum time-on period applies to all key audit partners. However, there are different cooling-off periods depending on the role of the key audit partner, as summarised below:

Role	Time-on and cooling-off periods
Engagement partner	Maximum 7 year time-on period 5 year cooling-off period
Individual responsible for the engagement quality control review	Maximum 7 year time-on period 3 year cooling-off period
Other key audit partners	Maximum 7 year time-on period 2 year cooling-off period

¹ A FMC reporting entity considered to have a higher level of public accountability is defined as a FMC reporting entity or a class of FMC reporting entity that is considered to have a higher level of public accountability than other FMC reporting entities:

- Under section 461K of the Financial Markets Conduct Act 2013; or
- By notice issued by the Financial Markets Authority (FMA) under section 461L(1)(1) of the Financial Markets Conduct Act 2013.

Information on FMC designations is available on the FMA website.

The maximum 7-year time-on period is calculated on a cumulative basis and need not be consecutive (see Q76). ~~In some jurisdictions, the new provisions will permit for a limited time the application of a cooling-off period shorter than five consecutive years (but no shorter than three consecutive years) with respect to an engagement partner (refer to Q8).~~ Combinations of roles are addressed in Q87.

~~Pursuant to paragraph 290.168, firms may have the opportunity for relief from the partner rotation requirements in the Code based on an exemption provided by the relevant regulator in their jurisdiction. Where such relief is available, the individual could remain as a key audit partner (for example, as the engagement partner) on the audit engagement in accordance with any conditions specified under such relief.~~

~~**Q3-Q5 are provided to illustrate the application of the requirements set out above. These questions are not intended to address all possible circumstances. The principles should be applied to different facts and circumstances.**~~

Q:3. Engagement Partner of a Subsidiary of a Public Interest Entity

Individual A has served as the engagement partner for the audit of a public interest entity (P) for seven years. Individual B has served as the engagement partner on the audit of a subsidiary (S) of P for seven years. How long is the cooling-off period for individuals A and B?

A: A cooling-off period of five ~~years~~ applies to individual A, the engagement partner responsible for the report that is issued on behalf of the firm for the audit of P. This engagement partner is sometimes referred to as the “lead audit engagement partner” in a group audit and would be required to serve a five-year cooling-off period from the audit of P.

The determination of the cooling-off period applicable to individual B should be approached from two different perspectives: the audit of S and the group audit of P.

From the perspective of the audit of S, if S is a public interest entity, individual B would be the engagement partner responsible for the report issued on public interest entity S and therefore would be required to serve a five-year cooling-off period from the audit of S (subject to proposed paragraph 290.163). If S is not a public interest entity, there is no cooling-off requirement for individual B in relation to the audit of S. However, individual B will be subject to the general provisions set out in proposed paragraphs 290.148 – 290.152.

From the perspective of the group audit of P, it is necessary to determine if individual B is a key audit partner for the audit of P. This determination would depend on, for example, the significance of the subsidiary and whether individual B makes key decisions or judgements with respect to the audit of the group. If individual B was considered to be a key audit partner with respect to the group audit of P, he or she is required to serve a two-year cooling-off period from the group audit of P. (See also Q5.) If individual B was not considered to be a key audit partner in relation to the group audit of P, there is no cooling-off requirement for individual B in relation to the group audit of P. However, individual B will be subject to the general provisions set out in proposed paragraphs 290.148 – 290.152.

Q:4. Engagement Partner on the Audit of a Public Interest Entity Moving to a Subsidiary Audit

Individual A has completed a cumulative period of seven years as engagement partner on the audit of a public interest entity (P). Could individual A participate in the audit of a subsidiary (S) of P for purposes of the group audit of P without completing the required cooling-off period of five years?

Commented [MP2]: Unaware of such an exemption being given in NZ? It is built into the legislation in Australia, but is rarely used. Shall I delete this

Commented [MP3]: Have deleted IESBA footnote reference that this may be a cooling off period of shorter than 5 years (but no shorter than 3 years)

Commented [MP4]: All paragraph references will be to the proposed revised sections – can I leave like this – or do I add proposed in front of each one until we have issued the standard in New Zealand?

A: No. Paragraph 290.27 of the extant Code states that:

(a) Where an audit client is a ~~listed~~-FMC reporting entity considered to have a higher level of public accountability, references to an audit client include its related entities (which include subsidiaries); and

(b) For all other audit clients, references to an audit client include related entities over which the client has direct or indirect control (which also would include subsidiaries).

Accordingly, individual A is subject to a five-year cooling-off period with respect to both P and S, as the reference to the audit client (P) also includes S. Individual A would therefore not be permitted under the Code to participate in the audit of S for purposes of the group audit of P without completing the required cooling-off period of five years (subject to proposed paragraph 290.163).

However, if the audit of S is undertaken for purposes other than the group audit of P (for example, a statutory audit of S where the audit evidence is not used in the group audit of P), A could participate in that audit of S without serving any cooling-off period, subject to consideration of threats and safeguards pursuant the general provisions in proposed paragraphs 290.148 – 290.152.

Q:5. Engagement Partner on the Audit of a Subsidiary Moving to the Audit of the Public Interest Entity Parent

Individual C has completed a cumulative period of seven years as engagement partner on the audit of a subsidiary (S) of a public interest entity (P). Could individual C participate in the group audit of P after completing the seven years on the audit of S?

A: It depends on whether (a) individual C was a KAP with respect to the group audit of P and (b) whether S is a ~~listed~~-FMC reporting entity considered to have a higher level of public accountability and, if so, whether it is material to P.

If individual C was considered to be a key audit partner with respect to the group audit of P, he or she would not be able to participate in the group audit of P until the completion of a two-year cooling-off period. If S is a public interest entity, individual C would be required to serve a five-year cooling-off period (subject to proposed paragraph 290.163) in relation to the audit of S.

If individual C was not considered to be a key audit partner with respect to the group audit of P, but S is a ~~listed~~-FMC reporting entity considered to have a higher level of public accountability and it is material to P, individual C would also not be able to participate in the group audit of P.² Under the related entity provision in paragraph 290.27, the reference to audit client (in this case, S) will also include P.³ Individual C would therefore not be permitted to participate in the group audit of P without completing the required cooling-off period of five years (subject to proposed paragraph 290.163).

In all other circumstances, P would not be considered to be part of the audit client (S) and individual C could participate in the group audit of P after serving seven years as engagement partner on the audit of S, subject to consideration of threats and safeguards pursuant the general provisions in proposed paragraphs 290.148 – 290.152.

Commented [MP5]: NZ change from listed – inconsistent here with PIE definition! – but amended this way for EQCR requirement.

² If S is material to P, it is likely that the engagement partner on S would be a key audit partner with respect to the group audit of P. However, this is not necessarily the case in all circumstances. This is because under the definition of a key audit partner in the Code, whether the individual is a key audit partner depends on whether he or she makes key decisions or judgements on significant matters with respect to the audit of the group, and not on whether S is material to P.

³ The definition of a related entity under the Code includes an entity that has direct or indirect control over the client if the client is material to such entity.

Q:65. Signing Partner Different from Engagement Partner

The Code defines the engagement partner as the partner or other person in the firm who is responsible for the engagement and its performance, and for the report that is issued on behalf of the firm, and who, where required, has the appropriate authority from a professional, legal or regulatory body to sign the audit report. In the situation where the partner who signs the audit report (the signing partner) is not the same individual as the engagement partner, which cooling-off provisions apply to the former?

A: The signing partner, if different, would normally also be treated as an engagement partner and be subject to the same requirement as the engagement partner.

~~In jurisdictions- Where~~ where more than one audit partner is required to sign the audit report, it may not be reasonable or appropriate to treat all the signing partners as engagement partners. In this case, determining which cooling-off provisions apply would depend on ~~jurisdictional~~ circumstances and the reasons why there are additional signing partner(s). At a minimum, however, the signing partner(s) would be considered to be key audit partners and therefore subject to a minimum two-year cooling-off period as applicable to the audit of a public interest entity.

Breaks in Service

Q:76. How do breaks in service affect the determination of time-on and cooling-off periods for an engagement partner, an engagement quality control reviewer or any other key audit partner for the audit of a public interest entity?

A: In calculating the time-on period, the count of years may be restarted if the break in service is equal to at least the cooling-off period determined in accordance with ~~proposed~~ paragraphs 290.155 to 290.157 as applicable to the role in which the individual served in the year immediately prior to the break in service. Breaks in service that are shorter than the required cooling-off period do not contribute to the consecutive cooling-off period. For example, if a key audit partner for the audit of a public interest entity has completed five years in the role and is off the engagement for one year due to a medical leave, the one year off does not count towards cooling off and the year the individual was not on the engagement team also does not count towards the cumulative time-on period. He or she could therefore return to the engagement as a key audit partner for a further two years (completing a total of seven cumulative years of service) before being required to serve the cooling-off period associated with his or her role on the engagement.

In contrast, if the key audit partner had acted as the individual responsible for the engagement quality control review for those five years, followed by three years off the engagement, then he or she will have cooled off and could return to the engagement for a further seven years.

The table below illustrates some examples showing how the cooling-off period would apply in the case of an audit of a public interest entity where “X” represents a year in which the individual was not a key audit partner on the audit. For the purposes of this table, “KAP” refers to an individual who was neither the engagement partner nor the individual responsible for the engagement quality control review.

Yr 1	Yr 2	Yr 3	Yr 4	Yr 5	Yr 6	Yr 7	Yr 8	Yr 9	Cooling-off period
------	------	------	------	------	------	------	------	------	--------------------

EP	EP	EP	EP	EP	EP	X	EP		5 consecutive years off at end of year 8 (Note 1)
EQCR	EQCR	EQCR	EQCR	X	X	EQCR	EQCR	EQCR	3 consecutive years off at the end of year 9 (Note 2)
KAP	KAP	KAP	X	KAP	KAP	X	KAP	KAP	2 consecutive years off at the end of year 9 (Note 3)
KAP	KAP	KAP	X	X					The KAP could return in year 6 for a further 7-year period (Note 4)

Commented [MP6]: Deleted footnote regarding shorter possible cooling off period

Notes

1. The one year off the engagement in year 7 does not constitute cooling-off as it is less than the five consecutive years off required to achieve cooling off for an EP. So, the individual reaches seven cumulative years on the engagement at the end of year 8 after which he or she must serve a cooling-off period of five consecutive years.
2. The two years off the engagement in years 5 and 6 do not constitute cooling-off as they are less than the three consecutive years off required to achieve cooling off for an EQCR. So, the individual reaches seven cumulative years on the engagement at the end of year 9, after which he or she must serve a cooling-off period of three consecutive years.
3. The two years off the engagement in years 4 and 7 do not constitute cooling-off as they do not add up to two consecutive years off required to achieve cooling for a KAP. So, the individual reaches seven cumulative years on the engagement at the end of year 9, after which he or she must serve a cooling-off period of two consecutive years.
4. The individual has effectively served a cooling-off period of two consecutive years in years 4 and 5 (even though not required by the Code as he or she had not completed 7 years on the audit) and therefore could return in year 6 for a further 7-year period.

Combination of Roles

Q:87. An individual has undertaken a combination of key audit partner roles on the audit of a public interest entity during the seven-year time-on period. How should the required cooling-off period be determined in those circumstances?

A: The number of required years off will be determined by the roles undertaken and the periods during which they were performed. This is illustrated in the table below. For the purposes of the table, "KAP" refers to an individual who was neither the engagement partner nor the individual responsible for the engagement quality control review. For simplicity, breaks in service (covered in Q76) are ignored.

Yr 1	Yr 2	Yr 3	Yr 4	Yr 5	Yr 6	Yr 7	Cooling-off period
KAP	KAP	KAP	EP	EP	EP	EP	5 consecutive years (Note 1)
KAP	KAP	KAP	EQCR	EQCR	EQCR	EQCR	3 consecutive years (Note 2)
EP	EP	EP	KAP	KAP	KAP	KAP	2 consecutive years (Note 3)
EQCR	EQCR	EQCR	EQCR	EP	EP	EP	5 consecutive years (Note 4)
EQCR	EQCR	EQCR	EQCR	EQCR	EP	EP	3 consecutive years (Note 5)
EP	EP	KAP	KAP	KAP	EP	EP	5 consecutive years (Note 1)

Notes

1. As the individual has served on the audit engagement for a total of seven cumulative years in a combination of roles during which he or she was the EP for four or more years, the individual must serve a cooling-off period of five consecutive years before he or she can return to the audit engagement (see [proposed](#) paragraph 290.158).
2. As the individual has served on the audit engagement for a total of seven cumulative years in a combination of roles during which he or she was the EQCR for four or more years, the individual must serve a cooling-off period of three consecutive years before he or she can return to the audit engagement (see [proposed](#) paragraph 290.159).
3. The individual has served on the audit engagement for a total of seven cumulative years but has not served as the EP or the EQCR for at least four of those seven years. Accordingly, the individual must serve a cooling-off period of two consecutive years before he or she can return to the engagement (see [proposed](#) paragraph 290.161).
4. The individual has served on the audit engagement for a total of seven cumulative years in a combination of EP and EQCR roles during which he or she was the EP for three years, the individual must serve a cooling-off period of five consecutive years before he or she can return to the audit engagement (see [proposed](#) paragraph 290.160(a)).
5. As the individual has served on the audit engagement for a total of seven cumulative years in a combination of EP and EQCR roles but was the EP for less than three years, the individual must serve a cooling-off period of three consecutive years before he or she can return to the audit engagement (see [proposed](#) paragraph 290.160(b)).

A full analysis of the possible combinations and the determination of the required cooling-off period is included in the Appendix.

Shorter Cooling-off Period Established by Law or Regulation

Q:98. [Proposed](#) paragraph 290.163 will have effect only for audits of financial statements for periods beginning prior to December 15, 2023. Does this mean that for audits of financial statements for periods beginning on or after December 15, 2023, the cooling-off requirement for engagement partners on the audit of a public interest entity will be five consecutive years in jurisdictions where a legislative body or regulator (or organisation authorised or recognised by such legislative body or regulator) has established a cooling-off period shorter than five consecutive years??

A: Yes. Proposed paragraph 290.163 is intended to facilitate the transition to the new cooling-off period of five consecutive years for engagement partners on audits of public interest entities in those jurisdictions where a shorter cooling-off period is currently specified by a legislative body or regulator (or organization authorized or recognized by such legislative body or regulator) in their jurisdictions, provided that the cooling-off period is no shorter than three consecutive years.

The IESBA has committed to review during this transitional period the revised long association provisions to take account of, among other things, relevant legislative and regulatory developments as well as experience of the application of the provisions in practice.

In New Zealand, neither the Financial Markets Authority nor the NZX have established a shorter cooling off period and therefore entities regulated by these regulators cannot apply a shorter cooling off period prior to 2023.

Other

Q:10. Implications of Involvement in a Half-year Review

A key audit partner signs a half-year review opinion in relation to a client that is a public interest entity, then another partner signs the opinion for the audit. Does the partner's service as engagement partner for the half-year review engagement constitute a year for the purposes of applying the rotation requirements?

A: Yes. The partner for the review engagement is also considered to have served one year for the purposes of applying the rotation provisions even if he or she was not the engagement partner for the audit of the financial statements.

Q:11. Implications of a Need to Re-audit a Prior Period?

A firm accepts a new public interest entity audit client that had previously been audited by another firm. In the course of auditing the current period's financial statements, it was determined that the newly engaged firm should re-audit the prior two periods. For the purposes of the partner rotation provisions of the Code, does this engagement constitute one year or three years of service by the key audit partners?

A: This constitutes one year for the purposes of determining when the individuals would need to rotate.

Q:12. Manager Becoming a Key Audit Partner

A manager served on the audit engagement team for a public interest entity audit client for five years before being promoted to partner. How many years may he or she serve on the engagement as a key audit partner for that audit client?

A: The rotation requirements in the Code apply to time spent as a key audit partner. In principle, the individual may serve seven years as a key audit partner. However, the general provisions in the Code indicate that in evaluating the threat created by long association, the overall length of an individual's association with the client, how long the individual has been on the engagement team and the roles that he or she has played should be taken into account (see proposed paragraph 290.149). A firm may decide that it is appropriate to rotate an individual off the audit team before the end of the seven-year period (or to serve a period off the engagement before re-joining the audit engagement team as a key audit partner).

Transition to New Provisions

[Note: Q132-Q175 below illustrate different transition scenarios with respect to an engagement partner. The same circumstances could arise with respect to an engagement quality control reviewer.]

Cooling-off Period

Q:132. The engagement partner for the audit of a public interest entity served for seven cumulative years in that role with the completion of the calendar year 2016 audit. The individual subsequently did not participate in the 2017 and 2018 audits. Would that individual be able to come back as engagement partner for the 2019 audit for a new seven-year term?

A: Yes. As the new provisions become effective only for audits of financial statements for periods beginning on or after December 15, 2018 (i.e., effectively beginning with calendar 2019 audits) and the individual has served the time-on limit of seven cumulative years with the 2016 audit, the current cooling-off requirement of two consecutive years applies. The individual would therefore have to cool off for the 2017 and 2018 audits and could begin a new seven-year term beginning with the calendar 2019 audit under the new provisions.

Q:14 What is the last date that the old rules (the two year cooling off period) apply, for an engagement partner for the audit of a public interest entity that has served for seven cumulative years in that role?

The new provisions become effective for audits of financial statements for periods beginning on or after December 15, 2018. The engagement partner must have completed a two-year cooling-off period under the old provisions before the new provisions come into effect, otherwise the new rules apply. This means that the last time that the engagement partner can rotate off, and have the old rules apply, will be for years ending before December 2017. When the year end is after December 2017, the individual cannot complete the cooling off period using the old rules before the new rules come into effect. Thereafter the new rules will apply. (Refer to Q16).

For example, if the individual served as engagement partner for the seventh consecutive year for the June 30, 2017 year end, the individual must rotate off the engagement. The new provisions do not become effective for audits of financial statements for periods beginning on or after December 15, 2018. This individual will have completed the two-year cooling off period (off for the audits for June 30, 2018 and June 30, 2019 year ends) before the effective date of the revised requirements. The June 2019 year end is for a period beginning before the effective date of the revised standard, and therefore the individual has completed cooling off before the new rules come into effect. The individual could then come back as EP on the engagement for a new seven-year term with the June 30, 2020 audit.

Q:153 The engagement partner for the audit of a public interest entity served for seven cumulative years in that role with the completion of the calendar year 2018 audit. How long should the individual cool off?

A: The new provisions become effective for audits of financial statements for periods beginning on or after December 15, 2018, i.e., effectively audits for calendar year 2019 and thereafter. This means that in jurisdictions where a legislative body or regulator (or organization authorized or recognized by such legislative body or regulator) has established a cooling-off period shorter than five consecutive years, the shorter cooling-off period may be applied starting with the calendar year 2019 audit in accordance with

Commented [MP7]: This is a New Zealand additional question created by staff to address concerns around the retrospective application of the revised requirements.

Feedback is sought as to how to simplify the matter.

paragraph 290.163 as long as that period is not shorter than three consecutive years (see Q 9). In other jurisdictions New Zealand, the five-year cooling-off requirement will need to be applied starting with the calendar year 2019 audit, i.e., the individual could only come back to the engagement in any key audit partner role for a new seven-year term with the 2024 audit.

The table below illustrates the latter situation, where “X” represents a year in which the individual was not a key audit partner on the audit:

2018 (Year 7)	2019	2020	2021	2022	2023	2024 (Year 1)	2025 (Year 2)
EP	X	X	X	X	X	KAP	KAP

Q:16.4 The engagement partner for the audit of a public interest entity served for seven cumulative years in that role with the completion of the calendar year 2017 audit. How long should the individual cool off?

A: The new provisions, as explained in Q153, would be equally applicable had the individual completed his or her seven cumulative years as engagement partner with the 2017 audit and commenced cooling off as required by the old provisions from the 2018 audit. The new provisions apply as the engagement partner had not completed a two year cooling-off period under the old provisions when the new provisions come into effect.

Q:175. The engagement partner for the audit of a public interest entity served for five years in that role with the completion of the calendar year 2017 audit. The individual subsequently did not participate in the 2018 and 2019 audits. Would that individual be able to come back as engagement partner for the 2020 audit for a new seven-year term (having cooled off for the 2018 and 2019 audits)?

A: No. The new provisions are effective for audits of financial statements for periods beginning on or after December 15, 2018. This means that from calendar 2019 audits, the new cooling-off provisions in the Code apply. Accordingly, if the engagement partner comes off the engagement before the full permitted seven-year time-on period is served, under the new provisions the full five-year cooling-off period applies in accordance with proposed paragraph 290.154 before the individual may come back to the engagement in any key audit partner role for a new seven-year time-on period.

In this case, the individual would therefore be able to serve as engagement partner for only an additional two years (i.e., for the 2020 and 2021 audits) before reaching the cumulative seven-year time-on period. He or she would then need to cool off for five consecutive years from the 2022 audit.

Alternatively, the individual could remain off the engagement for the 2020, 2021 and 2022 audits, reaching the five consecutive years cooling-off period applicable to engagement partners under the new provisions, and then come back to the 2023 audit in any key audit partner role for a new seven-year time-on period.

~~(In accordance with proposed paragraph 290.163, where a legislative body or regulator (or organization authorized or recognized by such legislative body or regulator) has specified a cooling off period shorter than five years for engagement partners, that alternative cooling off period may be substituted for the five years described in the above situation provided that this period is no shorter than three years. See Q 9 for further explanation.)~~

The tables below illustrates the two options, where “X” represents a year in which the individual was not a key audit partner on the audit. (For simplicity, [proposed](#) paragraph 290.163 is ignored.)

2017 (Yr 5)	2018	2019	2020 (Yr 6)	2021 (Yr 7)	2022	2023	2024	2025	2026	2027 (Yr 1)
EP	X	X	EP	EP	X	X	X	X	X	KAP

2017 (Yr 5)	2018	2019	2020	2021	2022	2023 (Yr 1)	2024 (Yr 2)	2025 (Yr 3)	2026 (Yr 4)	2027 (Yr 5)
EP	X	X	X	X	X	KAP	KAP	KAP	KAP	KAP

Additional Restrictions on Activities during the Cooling-off Period

Q:186. The 2017 calendar year audit will be the seventh year an individual has served as a key audit partner on the audit of a public interest entity. The individual then commences a cooling-off period starting with the 2018 audit. How should the provision regarding additional restrictions on activities during the cooling-off period be applied?

A: The new provisions on scope of activities apply to all key audit partners from the effective date, i.e., effectively beginning with calendar year 2019 audits. Accordingly, if a key audit partner has completed his or her seventh cumulative year of service with the 2017 audit and commenced a cooling-off period with the 2018 audit, he or she would be required to comply with paragraph 290.149 of the extant Code for the 2018 audit and [proposed](#) paragraph 290.164 of the new provisions for the 2019 audit and thereafter. Additional restrictions would apply in 2019. For example, during 2019 the individual would not be permitted to lead or coordinate the firm’s professional services to the audit client – this change would need managing in terms of a firm’s resource planning.

Appendix

Application of Provisions Regarding Service in a Combination of Roles (See Q8)

Number of Years During Time-on Period			Cooling-off (Years)	Proposed section 290 Para Ref.
Engagement Partner	Engagement Quality Control Reviewer	Other Key Audit Partner		
7	-	-	5	155
6	1	-	5	158
6	-	1	5	158
5	2	-	5	158
5	1	1	5	158
5	-	2	5	158
4	3	-	5	158
4	2	1	5	158
4	1	2	5	158
4	-	3	5	158
3	4	-	5	160(a)
3	3	1	5	160(a)
3	2	2	5	160(a)
3	1	3	5	160(a)
3	-	4	2	161
2	5	-	3	160(b)
2	4	1	3	160(b)
2	3	2	3	160(b)
2	2	3	3	160(b)
2	1	4	2	161
2	-	5	2	161
1	6	-	3	159
1	5	1	3	159
1	4	2	3	159
1	3	3	3	160(b)

1	2	4	2	161
1	1	5	2	161
1	-	6	2	161
-	7	-	3	156
-	6	1	3	159
-	5	2	3	159
-	4	3	3	159
-	3	4	2	161
-	2	5	2	161
-	1	6	2	161
-	-	7	2	157

LONG ASSOCIATION OF PERSONNEL WITH AN AUDIT CLIENT

This Questions and Answers (Q&A) publication is issued by the Staff of the International Ethics Standards Board for Accountants (IESBA). It is intended to assist national standards setters, firms, IFAC member bodies and others as they adopt and implement the revised long association provisions in extant Section 290 of the *Code of Ethics for Professional Accountants* (the Code) approved by the IESBA in December 2016. The revised provisions are set out in the January 2017 [close-off document](#) available on the IESBA website.

This publication is designed to highlight, illustrate or explain aspects of the revised partner rotation regime in extant Section 290, and thereby assist in their proper application.

This publication does not amend or override the Code, the text of which alone is authoritative. Reading this Q&A is not a substitute for reading the Code. The Q&As are not meant to be exhaustive and reference to the Code itself should always be made. This publication does not constitute an authoritative or official pronouncement of the IESBA.

Note

The revised long association provisions are currently being restructured in accordance with the new structure and drafting conventions of the Code. The restructuring will not change the substance of the provisions.

The restructured provisions are expected to be published as part of the restructured Code by the end of Q1 2018. This Q&A publication will be updated to align with the final restructured provisions and re-issued around the same time as the restructured Code.

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I. General – Audit Partner Rotation Provisions

Audit Partner Rotation Provisions for Public Interest Entities

- Q1:** In respect of an audit of a public interest entity, are all key audit partners subject to the same time-on and cooling-off periods?
- A:** The same maximum time-on period applies to all key audit partners. However, there are different cooling-off periods depending on the role of the key audit partner as summarized below:

Role	Time-on and cooling-off periods
Engagement partner	Maximum 7 year time-on period 5 year cooling-off period
Individual responsible for the engagement quality control review	Maximum 7 year time-on period 3 year cooling-off period
Other key audit partners	Maximum 7 year time-on period 2 year cooling-off period

The maximum 7-year time-on period is calculated on a cumulative basis and need not be consecutive (see Q6). In some jurisdictions, the new provisions will permit for a limited time the application of a cooling-off period shorter than five consecutive years (but no shorter than three consecutive years) with respect to an engagement partner (refer to Q8). Combinations of roles are addressed in Q7.

Pursuant to paragraph 290.168, firms may have the opportunity for relief from the partner rotation requirements in the Code based on an exemption provided by the relevant regulator in their jurisdiction. Where such relief is available, the individual could remain as a key audit partner (for example, as the engagement partner) on the audit engagement in accordance with any conditions specified under such relief.

Q2-Q4 are provided to illustrate the application of the requirements set out above. These questions are not intended to address all possible circumstances. The principles should be applied to different facts and circumstances.

Engagement Partner on a Subsidiary of a Public Interest Entity

- Q2:** Individual A has served as the engagement partner for the audit of a public interest entity (P) for seven years. Individual B has served as the engagement partner on the audit of a subsidiary (S) of P for seven years. How long is the cooling-off period for individuals A and B?
- A:** A cooling-off period of five years¹ applies to individual A, the engagement partner responsible for the report that is issued on behalf of the firm for the audit of P. This engagement partner is sometimes referred to as the “lead audit engagement partner” in a group audit and would be required to serve a five-year cooling-off period from the audit of P.

¹ In some jurisdictions, the new provisions will permit for a limited time the application of a cooling-off period shorter than five consecutive years (but no shorter than three consecutive years) with respect to an engagement partner (refer to Q8).

The determination of the cooling-off period applicable to individual B should be approached from two different perspectives: the audit of S and the group audit of P.

From the perspective of the audit of S, if S is a public interest entity, individual B would be the engagement partner responsible for the report issued on public interest entity S and therefore would be required to serve a five-year cooling-off period from the audit of S (subject to paragraph 290.163). If S is not a public interest entity, there is no cooling-off requirement for individual B in relation to the audit of S. However, individual B will be subject to the general provisions set out in paragraphs 290.148 – 290.152.

From the perspective of the group audit of P, it is necessary to determine if individual B is a key audit partner for the audit of P. This determination would depend on, for example, the significance of the subsidiary and whether individual B makes key decisions or judgments with respect to the audit of the group. If individual B was considered to be a key audit partner with respect to the group audit of P, he or she is required to serve a two-year cooling-off period from the group audit of P. (See also Q4.) If individual B was not considered to be a key audit partner in relation to the group audit of P, there is no cooling-off requirement for individual B in relation to the group audit of P. However, individual B will be subject to the general provisions set out in paragraphs 290.148 – 290.152.

Engagement Partner on the Audit of a Public Interest Entity Moving to a Subsidiary Audit

Q3. Individual A has completed a cumulative period of seven years as engagement partner on the audit of a public interest entity (P). Could individual A participate in the audit of a subsidiary (S) of P for purposes of the group audit of P without completing the required cooling-off period of five years?

A. No. Paragraph 290.27 of the extant Code states that:

- (a) Where an audit client is a listed entity, references to an audit client include its related entities (which include subsidiaries); and
- (b) For all other audit clients, references to an audit client include related entities over which the client has direct or indirect control (which also would include subsidiaries).

Accordingly, individual A is subject to a five-year cooling-off period with respect to both P and S, as the reference to the audit client (P) also includes S. Individual A would therefore not be permitted under the Code to participate in the audit of S for purposes of the group audit of P without completing the required cooling-off period of five years (subject to paragraph 290.163).

However, if the audit of S is undertaken for purposes other than the group audit of P (for example, a statutory audit of S where the audit evidence is not used in the group audit of P), A could participate in that audit of S without serving any cooling-off period, subject to consideration of threats and safeguards pursuant the general provisions in paragraphs 290.148 – 290.152.

Engagement Partner on the Audit of a Subsidiary Moving to the Audit of the Public Interest Entity Parent

Q4. Individual C has completed a cumulative period of seven years as engagement partner on the audit of a subsidiary (S) of a public interest entity (P). Could individual C participate in the group audit of P after completing the seven years on the audit of S?

- A.** It depends on whether (a) individual C was a KAP with respect to the group audit of P and (b) whether S is a listed entity and, if so, whether it is material to P.

If individual C was considered to be a key audit partner with respect to the group audit of P, he or she would not be able to participate in the group audit of P until the completion of a two-year cooling-off period. If S is a public interest entity, individual C would be required to serve a five-year cooling-off period (subject to paragraph 290.163) in relation to the audit of S.

If individual C was not considered to be a key audit partner with respect to the group audit of P, but S is a listed entity and it is material to P, individual C would also not be able to participate in the group audit of P.² Under the related entity provision in paragraph 290.27, the reference to audit client (in this case, S) will also include P.³ Individual C would therefore not be permitted to participate in the group audit of P without completing the required cooling-off period of five years (subject to paragraph 290.163).

In all other circumstances, P would not be considered to be part of the audit client (S) and individual C could participate in the group audit of P after serving seven years as engagement partner on the audit of S, subject to consideration of threats and safeguards pursuant the general provisions in paragraphs 290.148 – 290.152.

Signing Partner Different from Engagement Partner

- Q5:** The Code defines the engagement partner as the partner or other person in the firm who is responsible for the engagement and its performance, and for the report that is issued on behalf of the firm, and who, where required, has the appropriate authority from a professional, legal or regulatory body to sign the audit report. In the situation where the partner who signs the audit report (the signing partner) is not the same individual as the engagement partner, which cooling-off provisions apply to the former?

- A:** The signing partner, if different, would normally also be treated as an engagement partner and be subject to the same requirement as the engagement partner.

In jurisdictions where more than one audit partner is required to sign the audit report, it may not be reasonable or appropriate to treat all the signing partners as engagement partners. In this case, determining which cooling-off provisions apply would depend on jurisdictional circumstances and the reasons why there are additional signing partner(s). At a minimum, however, the signing partner(s) would be considered to be key audit partners and therefore subject to a minimum two-year cooling-off period as applicable to the audit of a public interest entity.

II. Breaks in Service

- Q6:** How do breaks in service affect the determination of time-on and cooling-off periods for an engagement partner, an engagement quality control reviewer or any other key audit partner for the

² If S is material to P, it is likely that the engagement partner on S would be a key audit partner with respect to the group audit of P. However, this is not necessarily the case in all circumstances. This is because under the definition of a key audit partner in the Code, whether the individual is a key audit partner depends on whether he or she makes key decisions or judgments on significant matters with respect to the audit of the group, and not on whether S is material to P.

³ The definition of a related entity under the Code includes an entity that has direct or indirect control over the client if the client is material to such entity.

audit of a public interest entity?

A: In calculating the time-on period, the count of years may be restarted if the break in service is equal to at least the cooling-off period determined in accordance with paragraphs 290.155 to 290.157 as applicable to the role in which the individual served in the year immediately prior to the break in service. Breaks in service that are shorter than the required cooling-off period do not contribute to the consecutive cooling-off period. For example, if a key audit partner for the audit of a public interest entity has completed five years in the role and is off the engagement for one year due to a medical leave, the one year off does not count towards cooling off and the year the individual was not on the engagement team also does not count towards the cumulative time-on period. He or she could therefore return to the engagement as a key audit partner for a further two years (completing a total of seven cumulative years of service) before being required to serve the cooling-off period associated with his or her role on the engagement.

In contrast, if the key audit partner had acted as the individual responsible for the engagement quality control review for those five years, followed by three years off the engagement, then he or she will have cooled off and could return to the engagement for a further seven years.

The table below illustrates some examples showing how the cooling-off period would apply in the case of an audit of a public interest entity where “X” represents a year in which the individual was not a key audit partner on the audit. For the purposes of this table, “KAP” refers to an individual who was neither the engagement partner nor the individual responsible for the engagement quality control review.

Yr 1	Yr 2	Yr 3	Yr 4	Yr 5	Yr 6	Yr 7	Yr 8	Yr 9	Cooling-off period
EP	EP	EP	EP	EP	EP	X	EP		5 consecutive years off at end of year 8 ⁴ (Note 1)
EQCR	EQCR	EQCR	EQCR	X	X	EQCR	EQCR	EQCR	3 consecutive years off at the end of year 9 (Note 2)
KAP	KAP	KAP	X	KAP	KAP	X	KAP	KAP	2 consecutive years off at the end of year 9 (Note 3)
KAP	KAP	KAP	X	X					The KAP could return in year 6 for a further 7-year period (Note 4)

Notes

1. The one year off the engagement in year 7 does not constitute cooling-off as it is less than the five consecutive years off required to achieve cooling off for an EP. So, the individual reaches

⁴ In some jurisdictions, the new provisions will permit for a limited time the application of a cooling-off period shorter than five consecutive years (but no shorter than three consecutive years) with respect to an engagement partner (refer to Q8).

seven cumulative years on the engagement at the end of year 8 after which he or she must serve a cooling-off period of five consecutive years.

2. The two years off the engagement in years 5 and 6 do not constitute cooling-off as they are less than the three consecutive years off required to achieve cooling off for an EQCR. So, the individual reaches seven cumulative years on the engagement at the end of year 9, after which he or she must serve a cooling-off period of three consecutive years.
3. The two years off the engagement in years 4 and 7 do not constitute cooling-off as they do not add up to two consecutive years off required to achieve cooling for a KAP. So, the individual reaches seven cumulative years on the engagement at the end of year 9, after which he or she must serve a cooling-off period of two consecutive years.
4. The individual has effectively served a cooling-off period of two consecutive years in years 4 and 5 (even though not required by the Code as he or she had not completed 7 years on the audit) and therefore could return in year 6 for a further 7-year period.

III. Combination of Roles

Q7: An individual has undertaken a combination of key audit partner roles on the audit of a public interest entity during the seven-year time-on period. How should the required cooling-off period be determined in those circumstances?

A: The number of required years off will be determined by the roles undertaken and the periods during which they were performed. This is illustrated in the table below. For the purposes of the table, “KAP” refers to an individual who was neither the engagement partner nor the individual responsible for the engagement quality control review. For simplicity, breaks in service (covered in Q6) are ignored.

Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Cooling-off Period ⁵	Note
KAP	KAP	KAP	EP	EP	EP	EP	5 consecutive years	(1)
KAP	KAP	KAP	EQCR	EQCR	EQCR	EQCR	3 consecutive years	(2)
EP	EP	EP	KAP	KAP	KAP	KAP	2 consecutive years	(3)
EQCR	EQCR	EQCR	EQCR	EP	EP	EP	5 consecutive years ⁶	(4)

⁵ In some jurisdictions, the new provisions will permit for a limited time the application of a cooling-off period shorter than five consecutive years (but no shorter than three consecutive years) with respect to an engagement partner (refer to Q8).

⁶ As part of its current project to revise its International Standard on Quality Control (ISQC) 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*, the International

Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Cooling-off Period ⁵	Note
EQCR	EQCR	EQCR	EQCR	EQCR	EP	EP	3 consecutive years	(5)
EP	EP	KAP	KAP	KAP	EP	EP	5 consecutive years	(1)

Notes

1. As the individual has served on the audit engagement for a total of seven cumulative years in a combination of roles during which he or she was the EP for four or more years, the individual must serve a cooling-off period of five *consecutive* years before he or she can return to the audit engagement (see paragraph 290.158).
2. As the individual has served on the audit engagement for a total of seven cumulative years in a combination of roles during which he or she was the EQCR for four or more years, the individual must serve a cooling-off period of three *consecutive* years before he or she can return to the audit engagement (see paragraph 290.159).
3. The individual has served on the audit engagement for a total of seven cumulative years but has not served as the EP or the EQCR for at least four of those seven years. Accordingly, the individual must serve a cooling-off period of two *consecutive* years before he or she can return to the engagement (see paragraph 290.161).
4. he individual has served on the audit engagement for a total of seven cumulative years in a combination of EP and EQCR roles during which he or she was the EP for three years, the individual must serve a cooling-off period of five *consecutive* years before he or she can return to the audit engagement (see paragraph 290.160(a)).
5. As the individual has served on the audit engagement for a total of seven cumulative years in a combination of EP and EQCR roles but was the EP for less than three years, the individual must serve a cooling-off period of three *consecutive* years before he or she can return to the audit engagement (see paragraph 290.160(b)).

A full analysis of the possible combinations and the determination of the required cooling-off period is included in the Appendix.

IV. Shorter Cooling-off Period Established by Law or Regulation

Q8: Paragraph 290.163 will have effect only for audits of financial statements for periods beginning prior to December 15, 2023. Does this mean that for audits of financial statements for periods beginning on or after December 15, 2023, the cooling-off requirement for engagement partners on the audit of a public interest entity will be five consecutive years in jurisdictions where a legislative body or

Auditing and Assurance Standards Board (IAASB) is examining how to address situations where an individual moves into an EQCR role on an audit engagement immediately after having served as EP on the same engagement.

regulator (or organization authorized or recognized by such legislative body or regulator) has established a cooling-off period shorter than five consecutive years?

- A:** Yes. Paragraph 290.163 is intended to facilitate the transition to the new cooling-off period of five consecutive years for engagement partners on audits of public interest entities in those jurisdictions where a shorter cooling-off period is currently specified by a legislative body or regulator (or organization authorized or recognized by such legislative body or regulator) in their jurisdictions, provided that the cooling-off period is no shorter than three consecutive years.

The IESBA has committed to review during this transitional period the revised long association provisions to take account of, among other things, relevant legislative and regulatory developments as well as experience of the application of the provisions in practice.

V. Other

Implications of Involvement in a Half-year Review

- Q9:** A key audit partner signs a half-year review opinion in relation to a client that is a public interest entity, then another partner signs the opinion for the audit. Does the partner's service as engagement partner for the half-year review engagement constitute a year for the purposes of applying the rotation requirements?

- A:** Yes. The partner for the review engagement is also considered to have served one year for the purposes of applying the rotation provisions even if he or she was not the engagement partner for the audit of the financial statements.

Implications of a Need to Re-audit a Prior Period

- Q10:** A firm accepts a new public interest entity audit client that had previously been audited by another firm. In the course of auditing the current period's financial statements, it was determined that the newly engaged firm should re-audit the prior two periods. For the purposes of the partner rotation provisions of the Code, does this engagement constitute one year or three years of service by the key audit partners?

- A:** This constitutes one year for the purposes of determining when the individuals would need to rotate.

Manager Becoming a Key Audit Partner

- Q11:** A manager served on the audit engagement team for a public interest entity audit client for five years before being promoted to partner. How many years may he or she serve on the engagement as a key audit partner for that audit client?

- A:** The rotation requirements in the Code apply to time spent as a key audit partner. In principle, the individual may serve seven years as a key audit partner. However, the general provisions in the Code indicate that in evaluating the threat created by long association, the overall length of an individual's association with the client, how long the individual has been on the engagement team and the roles that he or she has played should be taken into account (see paragraph 290.149). A firm may decide that it is appropriate to rotate an individual off the audit team before the end of the seven-year period (or to serve a period off the engagement before re-joining the audit engagement team as a key audit partner).

VI. Transition to New Provisions

[Note: Q12-Q15 below illustrate different transition scenarios with respect to an engagement partner. The same circumstances could arise with respect to an engagement quality control reviewer.]

Cooling-off Period

Q12: The engagement partner for the audit of a public interest entity served for seven cumulative years in that role with the completion of the calendar year 2016 audit. The individual subsequently did not participate in the 2017 and 2018 audits. Would that individual be able to come back as engagement partner for the 2019 audit for a new seven-year term?

A: Yes. As the new provisions become effective only for audits of financial statements for periods beginning on or after December 15, 2018 (i.e., effectively beginning with calendar 2019 audits) and the individual has served the time-on limit of seven cumulative years with the 2016 audit, the current cooling-off requirement of two consecutive years applies. The individual would therefore have to cool off for the 2017 and 2018 audits and could begin a new seven-year term beginning with the calendar 2019 audit under the new provisions.

Q13: The engagement partner for the audit of a public interest entity served for seven cumulative years in that role with the completion of the calendar year 2018 audit. How long should the individual cool off?

A: The new provisions become effective for audits of financial statements for periods beginning on or after December 15, 2018, i.e., effectively audits for calendar year 2019 and thereafter. This means that in jurisdictions where a legislative body or regulator (or organization authorized or recognized by such legislative body or regulator) has established a cooling-off period shorter than five consecutive years, the shorter cooling-off period may be applied starting with the calendar year 2019 audit in accordance with paragraph 290.163 as long as that period is not shorter than three consecutive years (see Q8). In other jurisdictions, the five-year cooling-off requirement will need to be applied starting with the calendar year 2019 audit, i.e., the individual could only come back to the engagement in any key audit partner role for a new seven-year term with the 2024 audit.

The table below illustrates the latter situation, where “X” represents a year in which the individual was not a key audit partner on the audit:

2018 (Year 7)	2019	2020	2021	2022	2023	2024 (Year 1)	2025 (Year 2)
EP	X	X	X	X	X	KAP	KAP

Q14: The engagement partner for the audit of a public interest entity served for seven cumulative years in that role with the completion of the calendar year 2017 audit. How long should the individual cool off?

A: The new provisions, as explained in Q13, would be equally applicable had the individual completed his or her seven cumulative years as engagement partner with the 2017 audit and commenced cooling off as required by the old provisions from the 2018 audit. The new provisions apply as the engagement partner had not completed a two year cooling-off period under the old provisions when the new provisions come into effect.

Q15: The engagement partner for the audit of a public interest entity served for five years in that role with the completion of the calendar year 2017 audit. The individual subsequently did not participate in the 2018 and 2019 audits. Would that individual be able to come back as engagement partner for the 2020 audit for a new seven-year term (having cooled off for the 2018 and 2019 audits)?

A: No. The new provisions are effective for audits of financial statements for periods beginning on or after December 15, 2018. This means that from calendar 2019 audits, the new cooling-off provisions in the Code apply. Accordingly, if the engagement partner comes off the engagement before the full permitted seven-year time-on period is served, under the new provisions the full five-year cooling-off period applies in accordance with paragraph 290.154 before the individual may come back to the engagement in any key audit partner role for a new seven-year time-on period.

In this case, the individual would therefore be able to serve as engagement partner for only an additional two years (i.e., for the 2020 and 2021 audits) before reaching the cumulative seven-year time-on period. He or she would then need to cool off for five consecutive years from the 2022 audit.

Alternatively, the individual could remain off the engagement for the 2020, 2021 and 2022 audits, reaching the five consecutive years cooling-off period applicable to engagement partners under the new provisions, and then come back to the 2023 audit in any key audit partner role for a new seven-year time-on period.

(In accordance with paragraph 290.163, where a legislative body or regulator (or organization authorized or recognized by such legislative body or regulator) has specified a cooling-off period shorter than five years for engagement partners, that alternative cooling-off period may be substituted for the five years described in the above situation provided that this period is no shorter than three years. See Q8 for further explanation.)

The tables below illustrates the two options, where “X” represents a year in which the individual was not a key audit partner on the audit. (For simplicity, paragraph 290.163 is ignored.)

2017 (Yr 5)	2018	2019	2020 (Yr 6)	2021 (Yr 7)	2022	2023	2024	2025	2026	2027 (Yr 1)
EP	X	X	EP	EP	X	X	X	X	X	KAP

2017 (Yr 5)	2018	2019	2020	2021	2022	2023 (Yr 1)	2024 (Yr 2)	2025 (Yr 3)	2026 (Yr 4)	2027 (Yr 5)
EP	X	X	X	X	X	KAP	KAP	KAP	KAP	KAP

Additional Restrictions on Activities during the Cooling-off Period

Q16: The 2017 calendar year audit will be the seventh year an individual has served as a key audit partner on the audit of a public interest entity. The individual then commences a cooling-off period starting with the 2018 audit. How should the provision regarding additional restrictions on activities during the cooling-off period be applied?

- A:** The new provisions on scope of activities apply to all key audit partners from the effective date, i.e., effectively beginning with calendar year 2019 audits. Accordingly, if a key audit partner has completed his or her seventh cumulative year of service with the 2017 audit and commenced a cooling-off period with the 2018 audit, he or she would be required to comply with paragraph 290.149 of the extant Code for the 2018 audit and paragraph 290.164 of the new provisions for the 2019 audit and thereafter. Additional restrictions would apply in 2019. For example, during 2019 the individual would not be permitted to lead or coordinate the firm's professional services to the audit client – this change would need managing in terms of a firm's resource planning.

Application of Provisions Regarding Service in a Combination of Roles

(See Q7)

Number of Years During Time-on Period			Cooling-off (Years) ⁷	Sec. 290 Para Ref.
Engagement Partner	Engagement Quality Control Reviewer	Other Key Audit Partner		
7	–	–	5	155
6	1	–	5	158
6	–	1	5	158
5	2	–	5	158
5	1	1	5	158
5	–	2	5	158
4	3	–	5	158
4	2	1	5	158
4	1	2	5	158
4	–	3	5	158
3	4	–	5	160(a)
3	3	1	5	160(a)
3	2	2	5	160(a)
3	1	3	5	160(a)
3	–	4	2	161
2	5	–	3	160(b)
2	4	1	3	160(b)
2	3	2	3	160(b)
2	2	3	3	160(b)
2	1	4	2	161

⁷ In some jurisdictions, the new provisions will permit for a limited time the application of a cooling-off period shorter than five consecutive years (but no shorter than three consecutive years) with respect to an engagement partner (refer to Q8).

Number of Years During Time-on Period			Cooling-off (Years) ⁷	Sec. 290 Para Ref.
Engagement Partner	Engagement Quality Control Reviewer	Other Key Audit Partner		
2	–	5	2	161
1	6	–	3	159
1	5	1	3	159
1	4	2	3	159
1	3	3	3	160(b)
1	2	4	2	161
1	1	5	2	161
1	–	6	2	161
–	7	-	3	156
–	6	1	3	159
–	5	2	3	159
–	4	3	3	159
–	3	4	2	161
–	2	5	2	161
–	1	6	2	161
–	–	7	2	157

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The objective of the IESBA is to serve the public interest by setting high-quality ethics standards for professional accountants and by facilitating the convergence of international and national ethics standards, including auditor independence requirements, through the development of a robust, internationally appropriate code of ethics.

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NZAuASB Board Meeting Summary Paper

AGENDA ITEM NO.	9.1
Meeting date:	26 July 2017
Subject:	Guidance for prescribers of assurance requirements on using the NZAuASB assurance standards
Date:	13 July 2017

Action Required

For Information Purposes Only

Agenda Item Objectives

To consider and provide feedback on the guidance for prescribers of assurance requirements

Background

1. The Board approved in February 2016 a project to develop guidance on the use of relevant standards and assurance products.
2. As the first step of this project, we developed general guidance on the use of the NZAuASB's assurance standards, which the Board approved in its July 2016 meeting. The general guidance is a useful part of the final guidance product and not intended for any specific user group, but to serve as the foundation of guidance for specific user groups.
3. In the Board's September 2016 meeting, the Board approved that the funders of not-for-profit entities (with a focus on registered charities) should be the first user-group for whom guidance on the NZAuASB assurance standards is to be prepared. The guidance for funders was approved in February 2017. The guide is now printed and ready to be distributed, and will be uploaded on our website in due course.
4. The Board agreed in February 2017 that the next user specific group to develop guidance for in relation to the use of relevant standards and assurance products, are prescribers of assurance engagements (e.g. policy makers and regulatory supervisors such as the FMA)

Update on the Project

5. Agenda item 9.2 includes the first draft of guidance for prescribers of assurance requirements. Similar to the guide for funders, the approach we adopted in developing this guide has been to start with a more comprehensive version first, with a view to simplify and shorten it to also produce a summary version.
6. The main objectives of the guide are to assist prescribers of assurance engagements to:
 - a. consider if an assurance engagement in accordance with the XRB assurance standards is the appropriate type of assignment for their circumstances
 - b. determine what different professional services are available under the XRB standards and which services are appropriate when prescribing an assurance engagement
 - c. appropriately describe such an engagement in terms of its requirements and terminology to ensure:
 - i. the engagement is consistent with the relevant XRB assurance standards (including professional ethical standards); and
 - ii. the correct description (e.g. accurate title for the engagement and the assurance practitioner, correct reference to the applicable standards etc) is used in relevant documents (e.g. legislation, regulations, contracts, funding agreements etc.).

Matters to consider

7. At this stage, we seek the Board's initial feedback on the content of the first draft of the (i.e. have all key matters been included, is it technically correct, is it not too difficult to follow, are there any matters that should be excluded, etc).

Material Presented

Agenda item 9.1	Board meeting summary paper guide of prescribers of assurance engagements
Agenda item 9.2	Guidance for prescribers of assurance engagements

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Introduction:

Regulators, government departments and others impose requirements for certain entities to arrange for a professional assignment over a particular matter of interest in order to increase the confidence and credibility of information. When such assignments are required or expected to be undertaken in accordance with standards issued by the New Zealand Auditing and Assurance Standards Board (NZAuASB), they are referred to as assurance engagements.

This document is intended to assist those who impose assurance requirements to:

- 1) consider if assurance engagements in accordance with the NZAuASB assurance standards are the type of assignment appropriate in their particular circumstances
- 2) determine what different professional services are available under the NZAuASB standards and which services are appropriate
- 3) appropriately describe such an engagement in terms of its requirements and terminology to ensure:
 - a. the engagement is consistent with the relevant NZAuASB assurance standards (including professional ethical standards); and
 - b. the correct description (e.g. accurate title for the engagement and the assurance practitioner, correct reference to the applicable standards etc) is used in relevant documents (e.g. legislation, regulations, contracts, funding agreements etc.).

This guidance is helpful when:

- Proposing new legislation that will require assurance (especially those expected to be undertaken by practitioners who need to comply with the NZAuASB standards).
- Revising and clarifying existing legislation that requires assurance.
- Drafting documentation in relation to expected professional assignments (e.g. when imposing a requirement to arrange for a professional assignment as part of funding criteria).
- Seeking professional services to undertake an assignment.

The guidance has two parts:

- Part 1: provides an overview of what is assurance and when is it used.
- Part 2: considers the characteristics of an assurance engagement and the importance of using terminology and specifications that are consistent with the applicable NZAuASB assurance standards.

Part 1) What is assurance and when is it used?

The demand for assurance

A user of information demands assurance as a method to enhance the credibility of information that is prepared by someone else. An overview of this relationship, how information is prepared and how an assurance engagement helps to enhance its credibility is demonstrated in diagram 1 on page 5 of this Guide.

What is an assurance engagement?

Assurance engagements performed in accordance with the NZAuASB standards are one type of professional assignment that can be undertaken to enhance credibility or reliability of communications between different parties (refer diagram 1 on page 5). It is important to note that the term “assurance engagement” has a specific meaning in the context of the NZAuASB assurance standards that may be different from its everyday usage. An assignment can only be described as an “assurance engagement” when all the following conditions are met.

- 1) There are at least three parties: a responsible party, an intended user and an assurance practitioner.
- 2) The assurance practitioner plans and performs the engagement to obtain sufficient appropriate evidence that:
 - (i) the underlying subject matter (USM) is appropriately measured/evaluated against the criteria (see diagram 1 on page 5 to understand these terms), and
 - (ii) the resulting subject matter information (SMI) is free from material misrepresentation.
- 3) The engagement is conducted in accordance with the applicable NZAuASB assurance standard(s) including professional and ethical standards and quality control standards.

Is an assurance engagement what you are looking for?

- 1) Consider the objective of requiring a professional assignment and the users who will benefit from the assignment.
- 2) Consider if there is a statutory reason for requiring such an assignment to be undertaken in accordance with the NZAuASB assurance standards.
- 3) Consider if the expected type of assignment is one that is undertaken by professional practitioners that comply with the NZAuASB standards (e.g. professional accountants who are members of professional accounting bodies are required to comply with the NZAuASB standards) or by practitioners that undertake assignments in accordance with frameworks other than the NZAuASB assurance standards (e.g. standards issued by the International Organization for Standardization (ISO) or Standards New Zealand).
- 4) Consider the expectations from an assurance engagement and assess if these align with what an assurance engagement can deliver.
- 5) Consider if an agreed upon procedures (AUP) engagement¹ is more appropriate in the circumstances.

¹An AUP engagement involves a practitioner performing procedures that have been agreed to by the practitioner, the entity and any appropriate third parties, and reporting on the factual findings based on the procedures performed. In conducting an AUP engagement, the practitioner **does not express an opinion**. Users of the AUP report assess for themselves the factual findings based on the procedures performed and draw their own conclusions. AUP engagements are not currently included in the NZAuASB’s mandate, more

We s recommend that an organisation obtains professional advice (for example, by consulting professional accounting bodies) in determining if the NZAuASB standards provide an appropriate framework for addressing the specific needs it intends to address.

Diagram 1: Overview of how information is prepared and how assurance engagements help in enhancing credibility

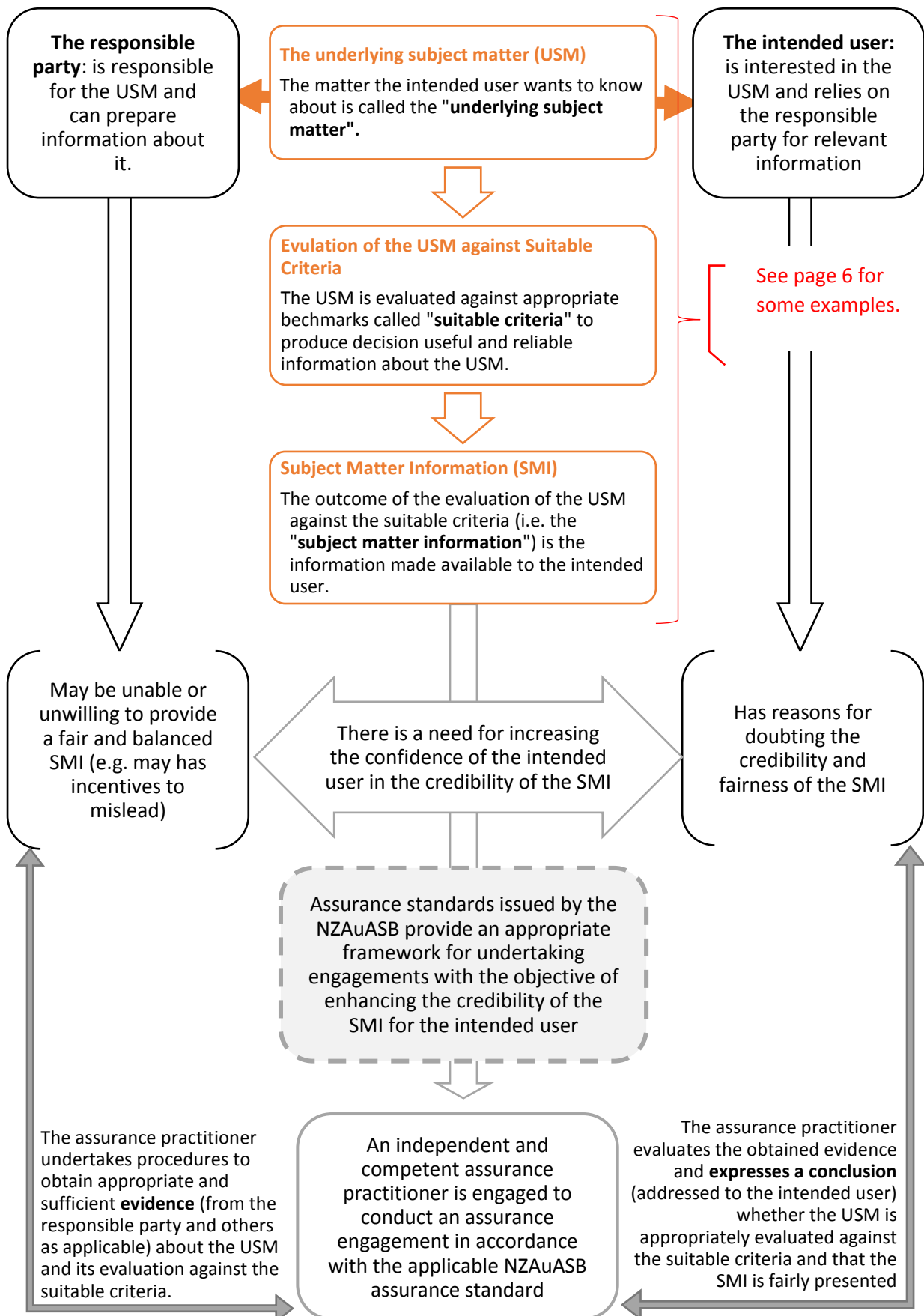
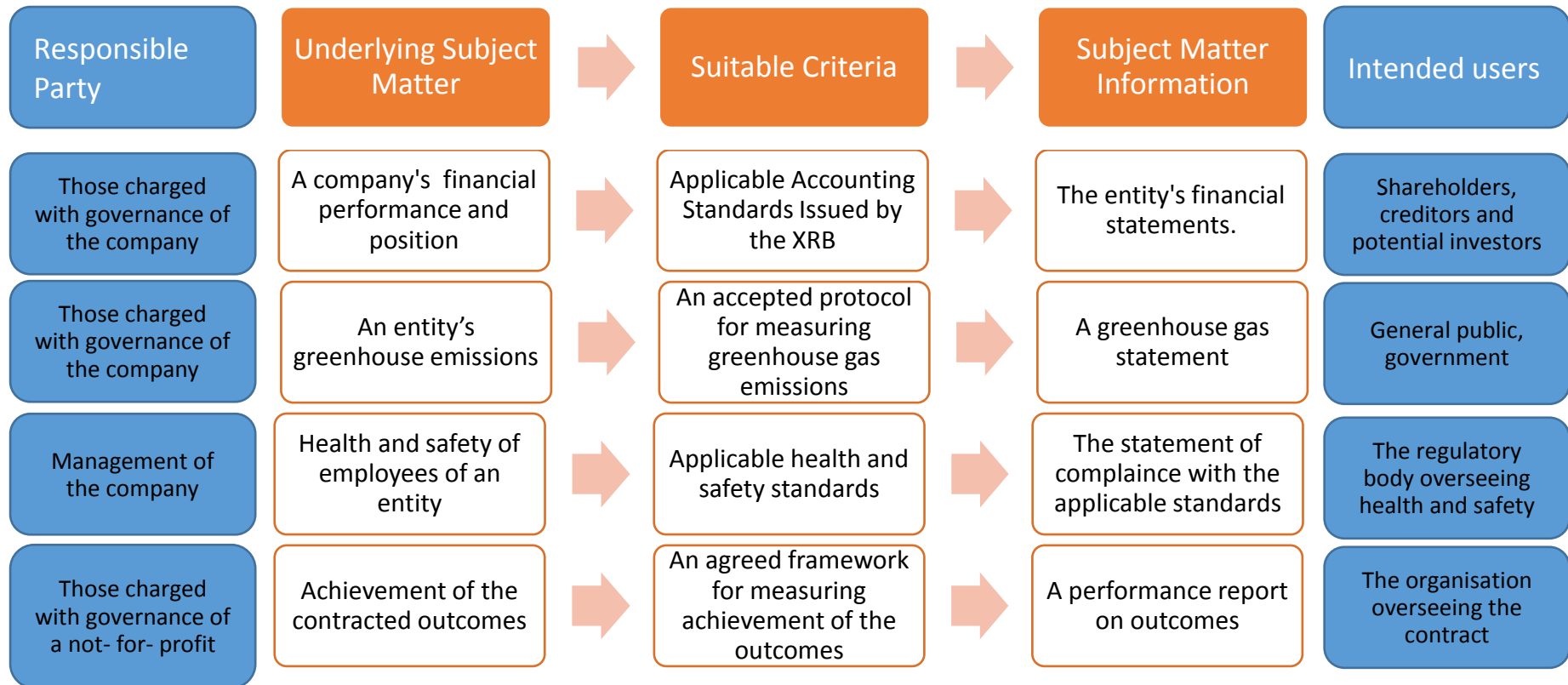


Diagram 2: Examples of information relationships between intended users and responsible parties



PART 2) Describing an assurance engagement in accordance with the NZAuASB's standards

If you require an assurance engagement, you will need to describe and specify the scope of the required assurance engagement accurately and ensure its consistency with the NZAuASB assurance standards. It is as important to use correct terminology to describe the engagement. Using terminology that is inconsistent with how specific terms are defined in the NZAuASB assurance standards could lead to a difference in expectations between you and the assurance practitioner.

The specification includes the following considerations.

- The level of assurance.
- The NZAuASB assurance standards that are most appropriate in the circumstances.
- The qualifications or credentials of the potential assurance practitioners.
- The appropriateness of the underlying subject matter and availability of suitable criteria for its evaluation.
- Aligning the specifications of expected assurance engagements with the relevant NZAuASB standards.
- Using correct terminology when referring to auditing and assurance standards issued by the NZAuASB.

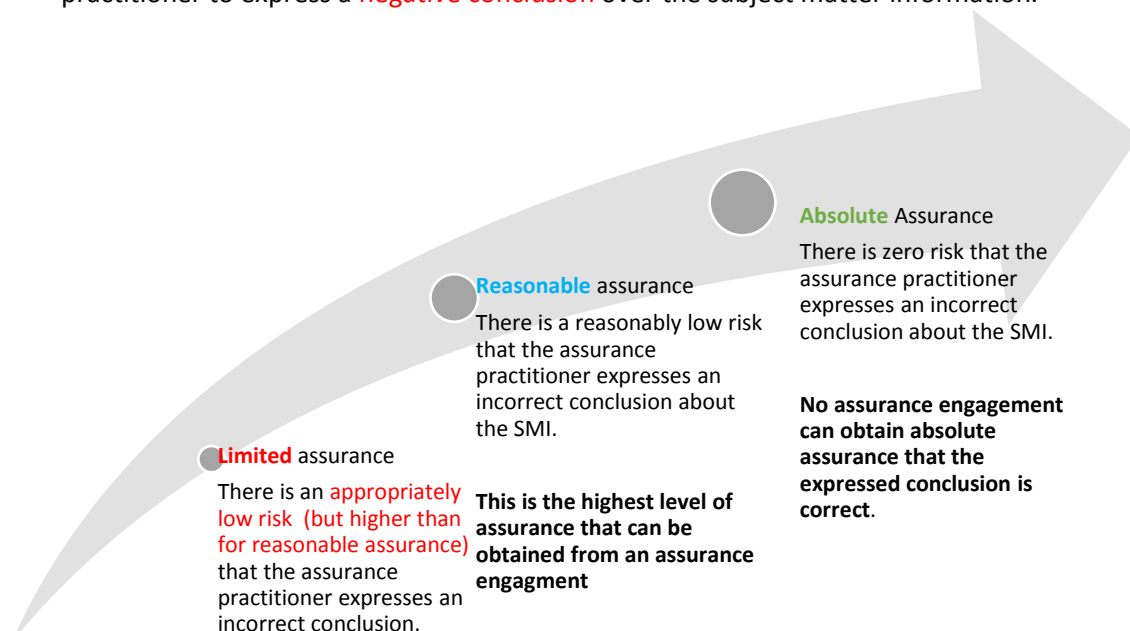
Levels of assurance

No assurance practitioner can obtain absolute assurance that the SMI is appropriately prepared and presented because:

- It is rarely attainable or cost beneficial to verify/test/evaluate every single element or component of the USM or the SMI. As a result:
 - i. The assurance practitioner considers materiality of the various elements and components of the USM and the SMI and focuses on those that if misrepresented could reasonably be expected to influence relevant decisions of the intended users, based on the SMI.
 - ii. The assurance practitioner applies selective testing to obtain evidence.
- Much of the evidence available to the assurance practitioner is persuasive rather than conclusive.
- The assurance practitioner applies professional judgement in gathering and evaluating evidence.
- The characteristics of the underlying subject matter when evaluated against suitable criteria may prevent the ability to draw an absolutely accurate conclusion. For example, the evaluation may involve the use of estimation and judgement.

The NZAuASB Framework for Assurance Engagements identifies two levels of assurance:

- **Reasonable assurance engagement** where a **high** level of assurance, which is less than absolute assurance, is obtained by the assurance practitioner from obtaining sufficient and appropriate evidence, which then allows the assurance practitioner to express a **positive opinion** over the subject matter information.
- **Limited assurance engagement** where a **meaningful level of assurance**, which is more than inconsequential but is less than reasonable assurance, is obtained by the assurance practitioner from obtaining sufficient and appropriate evidence, which then allows for the assurance practitioner to express a **negative conclusion** over the subject matter information.



Because the level of assurance obtained in a limited assurance engagement is lower than in a reasonable assurance engagement, the procedures the practitioner performs in a limited assurance

engagement vary in nature and timing from, and are less in extent than for, a reasonable assurance engagement.

The following table compares reasonable assurance with limited assurance:

Reasonable Assurance Engagement	Limited Assurance Engagement
A reasonable assurance engagement is designed to provide a reasonable level of assurance	A limited assurance engagement is designed to provide only limited assurance
The reasonable assurance report opinion : Expressed in positive form “...In our opinion, the subject matter information present fairly... ”	The limited assurance engagement conclusion : Expressed in the negative form “...based on the work performed, as described in the report, nothing has come to our attention... ”
Provides a high but not absolute level of assurance	Provides a lower level of assurance than from a reasonable assurance engagement
Assurance that the subject matter information is not materially misrepresented	Increased risk that assurance practitioner may not become aware of significant misrepresentation in the subject matter information
Drives a higher level of “Work Effort”	Drives a lower level of “Work Effort”

A selection between a limited level of assurance and a reasonable level of assurance is principally based on a cost-benefit analysis.

- A limited assurance may cost less and is usually completed in a shorter period of time but it provides limited assurance about the subject matter information.
- A reasonable assurance may cost more and is usually completed in a longer period of time but it provides reasonable assurance about the subject matter information.

Appendix 1 includes examples to assist in understanding the differences between a limited and reasonable assurance engagement.

The NZAuASB assurance standards

The NZAuASB assurance standards can be divided into the following two categories.

- 1) Standards for assurance engagements over historical financial information²
- 2) Standards for assurance engagements on any other subject matter.

Assurance engagements over historical financial information are either:

- an **audit** in accordance with the International Standards on Auditing (New Zealand) (ISAs (NZ)), or
- a **review** in accordance with the International Standards on Review Engagements (New Zealand) (ISREs (NZ)) or NZ SRE

An **audit** is an assurance engagement where the subject matter information is the financial statements³ of an entity. The purpose of an audit is for the assurance practitioner to:

- obtain **reasonable** assurance that the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework (the criteria); and
- express an opinion in a written report addressed to intended users that the financial statements are free from material misstatements (the audit report).

A review is also an assurance engagement where the subject matter information is the financial statements of an entity. However, a review provides **limited** assurance to the intended users of the financial statements.

The following exhibit summarises how a review engagement compares to audit.

Title of the Engagement	Standard	Level of Assurance	Work effort	Report
Audit	ISAs (NZ)	Reasonable	Has high work effort including Risk assessment and procedures that respond to the risks identified	Opinion expressed in positive form “...In our opinion , the financial statements present fairly ...”
Review	ISRE (NZ) NZ SRE	Limited	Has lower work effort (compared to an audit) and includes primarily enquiry (from management) and analysis of financial information (analytical review)	Conclusion expressed in the negative form “...based on the work performed, as described in the report, nothing has come to our attention ...”

² Historical financial information is information expressed in financial terms in relation to a particular entity, derived primarily from that entity’s accounting system, about economic events occurring in past time periods or about economic conditions or circumstances at points in time in the past.

³ A structured representation of historical financial information, including related notes, intended to communicate an entity’s economic resources or obligations at a point in time or the changes therein for a period of time in accordance with a financial reporting framework. The related notes ordinarily comprise a summary of significant accounting policies and other explanatory information. The term “financial statements” ordinarily refers to a complete set of financial statements as determined by the requirements of the applicable financial reporting framework, but can also refer to a single financial statement.

Assurance over all other types of subject matters (other than “historical financial information”) is dealt with under “**Other Assurance Engagement**” standards. These standards are a series of assurance standards that can be applied to wide range of subject matters. ISAE (NZ) 3000 (Revised), *Assurance Engagements Other than Audits or Reviews of Historical Financial Information*, is the umbrella standard for other assurance engagements, and is to be used with topic specific standards where relevant. The NZAuASB has issued the following subject matter specific other assurance standards:

- SAE 3100 (Revised), *Compliance Engagements*
- SAE 3150 (Revised), *Assurance Engagements on Controls*
- ISAE 3402, *Assurance Reports on Controls at a Service Organisation*
- ISAE 3410, *Assurance Engagements on Greenhouse Gas Statements*
- ISAE 3420, *Assurance Engagements to Report on the Compilation of Pro Forma Financial Information Included in a Prospectus*

All **other assurance engagements** can be undertaken as **reasonable** or **limited** assurance engagements.

Appendix 2 provides a diagram to help identify the appropriate NZAuASB assurance standard applicable to a required assurance engagement.

We recommend you obtain professional advice (for example, by consulting professional accounting bodies) in determining the appropriate “other assurance engagement standard” applicable to the engagement being considered

The eligibility of assurance practitioners

To conduct an assurance engagement in accordance with the NZAuASB standards, the assurance practitioner needs to:

- have competence in assurance skills and techniques and sufficient competence in the USM and its measurement or evaluation against suitable criteria;
- comply with the ethical requirements for an assurance practitioner; and
- comply with the quality control standards for an assurance practitioner and quality control requirements for a firm undertaking assurance engagements.

In New Zealand, the NZAuASB is responsible for setting the ethical and quality control requirements for an assurance practitioner who is required to, , conduct an assurance engagement in accordance with the NZAuASB assurance standards. The NZAuASB has currently issued the following two Professional and Ethical Standards:

- Professional and Ethical Standard (PES) 1 (Revised) , *Code of Ethics for Assurance Practitioners*
- Professional and Ethical Standard 3 (PES 3), *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance Engagements*

Audits or **reviews** of historical financial information **can only** be undertaken by assurance practitioners who are competent in both assurance skills and financial reporting and comply with the above two professional and ethical standards. As the auditing and assurance standards are primarily developed for assurance practitioners who are professional accountants, members of professional accounting bodies (such as the New Zealand Institute of Chartered Accountants and CPA Australia) are required to comply with the NZAuASB standards (including the Professional and Ethical Standards) when they undertake an assurance engagement. The following recognitions are granted to those assurance practitioners who provide assurance services over the financial statements of an entity in accordance with the NZAuASB assurance standards :

Recognition Title	Recognising Entity	Description
Licensed Auditor	The Financial Market Authority	This is the highest level of a statutory recognition an assurance practitioner auditing or reviewing the financial statements may obtain in New Zealand. A Licensed auditor is allowed to audit or review (in accordance with the NZAuASB assurance standards) the financial statements of FMC Reporting entities.
Qualified Auditor	The Chartered Accountants of Australia and New Zealand (CAANZ)	CAANZ members who are recognised as “qualified auditors” are allowed to audit or review (in accordance with the NZAuASB assurance standards) the financial statements of Registered Charities with statutory required audits or reviews.
A chartered Accountant with a Certificate of Public Practice (CPP)	CAANZ, and CPA Australia	This is the starting level of professional recognition for a chartered accountant who provides assurance services over the financial statements. A CPP holder is allowed to conduct audit and review (in accordance with the NZAuASB assurance standards) on financial statements for all entities, except for those that are restricted to Licensed or Qualified Auditors.
The Auditor-General	The Public Audit Act 2001	The Auditor-General is responsible for auditing all public entities.

For assurance engagements other than audits or reviews of historical financial information, ISAE (NZ) 3000 (Revised) requires the assurance practitioner to:

- 1) Comply with PES 1 (Revised), or other professional requirements, or requirements imposed by law or regulation, that are at least as demanding.
- 2) Be a member of a firm that applies PES 3, or other professional requirements, or requirements in law or regulation, that are at least as demanding as PES 3.
- 3) Have competence in assurance skills and techniques developed through extensive training and practical application; and
- 4) Have sufficient competence in the underlying subject matter and its measurement or evaluation to accept responsibility for the assurance conclusion.

Members of professional accounting bodies in New Zealand who are recognised as assurance practitioners⁴ are in an established position in relation to the compliance with ethical and quality control requirements for an assurance engagement.

NZAuASB standards for assurance engagements **other than** audit or a review of historical financial information may be used by individuals who are not professional accountants, but they can only assert compliance with those standards if they comply with rules of professional ethical and quality control standards that are at least as demanding as those issued by the NZAuASB.

We recommended you obtain professional advice (for example, by consulting the professional accounting bodies) in determining the eligibility of a potential assurance practitioner for undertaking the engagement being considered.

⁴ Please note that membership of a professional accounting body does not mean that the member is eligible for undertaking an assurance engagement. In addition to such membership, members will need to have the certificate of public practice for an assurance practitioner and be subjected to initial and continuing professional development as well as ongoing monitoring and disciplinary regimes to ensure the quality of their assurance services and their compliance with professional and ethical standards.

The appropriateness of the underlying subject matter and availability of suitable criteria for its evaluation.

An assurance engagement can only be undertaken over an underlying subject matter that:

- is identifiable and measurable against suitable criteria, and
- can be subjected to procedures to gather evidence sufficient to support the required assurance conclusion.

Existence of suitable criteria is a fundamental element of an assurance engagement. Suitable criteria⁵ are required for reasonably consistent measurement or evaluation of the underlying subject matter. Without the frame of reference provided by suitable criteria, any conclusion is open to individual interpretation and misunderstanding. Without suitable criteria, it is not feasible to produce subject matter information from the underlying subject matter which can be useful between individuals or organisations. Therefore, it is important for the entity requiring an assurance engagement to consider (and where appropriate specify) the suitable criteria for the assurance engagement it is prescribing.

Another important matter to consider is the availability of relevant evidence. Evidence is information used by the assurance practitioner in arriving at the assurance practitioner's conclusion. The prescribing entity will need to consider whether the assurance practitioner can reasonably be expected to be able to:

- obtain the evidence needed to support the assurance practitioner's conclusion, and
- have access to records, documentation and other information the assurance practitioner may require as evidence to complete the engagement.

⁵ For more information on suitable criteria please refer to ISAE (NZ) 3000 (Revised), paragraphs A45 to A50.

Using correct terminology when referring to assurance standards issued by the NZAuASB

As this guide explains, some terms (such as audit and auditor, review, assurance engagement, reasonable and limited assurance etc.) have specific meanings under the NZAuASB assurance standards. Unless these terms are used carefully, misleading information could be communicated to users. For instance, the terms “audit” and “assurance” are occasionally used in a way that is inconsistent between:

- the level of assurance that is **needed**,
- the level of assurance that is **requested**, and
- the level of assurance that is **provided**.

The following examples illustrate this:

- Some requirements imposed by entities are either not encapsulated by the NZAuASB standards or have a different meaning/interpretation to those intended by the imposing entity. For example, the assurance practitioner may be required to “certify” certain information. Certification is not a term used in the NZAuASB assurance standards as it implies “absolute assurance”. As explained, assurance engagements under the NZAuASB do not provide an absolute level of assurance. The correct terminology to use is to “obtain reasonable assurance”.
- The term “verification” has been used in connection with engagements required to be undertaken in accordance with the NZAuASB assurance standards. However, verification is a term that is most commonly used in relation to agreed-upon procedures engagements (that are not assurance engagements and do not involve obtaining any assurance by the assurance practitioner).
- The terms audit, auditor and review are sometimes inappropriately used. For example, an auditor is required to undertake a “review” and to provide an opinion that financial statements are “free from material misstatements”, instead of requiring a review in accordance with the IRSE (NZ) by an independent assurance practitioner to provide limited assurance that the financial statements are not materially misstated.

It is important that engagement titles and associated terminology are used consistently with the applicable NZAuASB assurance standards. The following table may be helpful in using the correct terminology in describing assurance engagements.

Subject Matter	Level of assurance	Title of the engagement	Title of the assurance practitioner	Applicable suite of standards	Applicable professional and ethical standards
Historical financial information	Reasonable	Audit	The independent auditor	ISAs (NZ)	PES 1 (Revised) and PES 3
	Limited	Review	The independent assurance practitioner	ISREs (NZ) and NZ SRE	
Other subject matters	Reasonable	Reasonable Assurance Engagement	The independent assurance practitioner	ISAEs (NZ) and SAEs (NZ)	PES 1 (Revised) and PES 3 or similar standards that are at least as demanding as PES 1 and PES 3
	Limited	Limited Assurance Engagement	The independent assurance practitioner	ISAEs (NZ) and SAEs (NZ)	

We recommended that you obtain professional advice (for example, by consulting professional accounting bodies) to ensure appropriate terminology is used in describing the required assurance engagement.

Appendix 1: Reasonable Vs Limited Assurance Engagements:

An assurance practitioner is currently assessing two properties (referred to as property A and property B) to provide assurance that these properties are not leaky. For property A, the assurance practitioner is engaged to provide limited assurance that a building is not leaky while for the property B the assurance practitioner is required to provide reasonable assurance that the building is not leaky.

Limited assurance over building A

For building A, the assurance practitioner obtains evidence that the building is not leaky by:

- Receiving an owner's briefing, sourcing documents, meeting building occupants, visual building inspection inside and out.
- Non-invasive investigation of moisture ingress to identify potential problem locations.

The assurance practitioner uses his professional knowledge and expertise in analysing the result of performed procedures. The assurance practitioner concludes that the results do not indicate that the building A has significant leaking problems. The assurance practitioner prepares the assurance report and concludes that:

“based on the work performed, as described in the report, nothing has come to my attention to indicate that the building is leaky”

Reasonable assurance over building B

For building B, the assurance practitioner obtains evidence that the building is not leaky by:

- Performing Invasive investigation of moisture ingress of the building with focus on those areas with higher risk of leak.
- Undertaking a sample of timber testing to ensure that the timber structure is not significantly affected by moisture.

The assurance practitioner uses his professional knowledge and expertise in analysing the result of performed procedures. The assurance practitioner concludes that based on performed procedures he/she has obtained sufficient appropriate evidence that the building is not leaky. The assurance practitioner prepares the assurance report and provides an opinion that:

“based on the work performed, as described in the report, in my opinion the building is not a leaky building in any significant manner”

The table on next page provides an overview of the differences between these two reports.

Comparison between the limited assurance engagement and reasonable assurance engagement		
	Limited assurance over building A	Reasonable assurance over building B
Level of assurance provided	<p>The intended user (e.g. a potential buyer) can take limited assurance that the building is not a leaky building.</p> <p>This is because a professional assurance practitioner with adequate knowledge and skills (e.g. with a good understanding of the leak risk factors relating to the building’s design, common areas affected by water leaking problems, etc) has performed procedures that reduces the likelihood of the building being leaky.</p> <p>An experienced building inspector is likely to identify indications of moisture problems by performing careful visual inspection. A potential buyer is likely to obtain confidence from knowing that the assurance practitioner visual inspection of the building has not identified any moisture problem indicators.</p>	<p>The intended user (e.g. a potential buyer) can take reasonable (but not absolute) assurance that the building is not a leaky building.</p> <p>This is because a professional assurance practitioner with adequate knowledge and skills (e.g. with a good understanding of the leak risk factors relating to the building’s design, common areas affected by water leaking problems, etc) has obtained sufficient and appropriate evidence to provide reasonable assurance that the building is not leaky.</p> <p>A potential buyer can obtain a reasonable level of confidence that the building is not leaky.</p>
The relationship between the level of assurance and undertaken assurance work	<p>The limited scope of assessment for a limited assurance engagement means that there is a higher risk that a significant issue is not identified. The building inspector can only provide limited assurance that the house is not leaky because:</p> <ul style="list-style-type: none"> • Damage can be hidden and may not be obvious during a visual examination. • The degree of confidence obtained from non-invasive moisture detecting techniques is limited. 	<p>The reasonable assurance engagement should be planned and performed to reduce the risk of a significant issue in the subject matter information being undetected to a reasonably low level. The building inspector can provide a higher level of assurance as the nature and extent of undertaken procedures significantly reduces the risk of a significant leak not being identified.</p> <p>It must be noted that the provided assurance is high but not absolute. For example, use of sampling in undertaking invasive moisture tests provides high but not absolute confidence that the building is not leaky.</p>

Appendix 2: Identifying the NZAuASB assurance standard(s) that are applicable to the required engagement

